

Audit

Report



OFFICE OF THE INSPECTOR GENERAL

MISSILE PROCUREMENT APPROPRIATIONS, AIR FORCE

Report Number 93-053

February 12, 1993

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Department of Defense

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The following acronyms are used in this report.

ACM.....	Advanced Cruise Missile
AFB.....	Air Force Base
AMRAAM.....	Advanced Medium Range Air-to-Air Missile
DFAS.....	Defense Finance and Accounting Service
GAO.....	General Accounting Office
"M" Account.....	Merged Account
MPAAF.....	Missile Procurement Appropriations, Air Force
NULO.....	Negative Unliquidated Obligation
OMB.....	Office of Management and Budget
SRMU.....	Solid Rocket Motor Upgrade
U.S.C.....	United States Code



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

February 12, 1993

MEMORANDUM FOR COMPTROLLER OF THE DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on the Missile Procurement Appropriations,
Air Force (Report No. 93-053)

This final report is provided for your information and use. The report resulted from our audit of the Missile Procurement Appropriations, Air Force, for FYs 1987 and 1988. Management comments on a draft of this report were considered in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Therefore, we request that the Comptroller of the Department of Defense provide final comments on the unresolved recommendations by April 13, 1993. The "Status of Recommendations" section at the end of Finding A lists unresolved recommendations and the specific requirements for your comments.

As required by DoD Directive 7650.3, the comments must indicate concurrence or nonconcurrence with the findings and each recommendation. If you concur, describe the corrective actions taken or planned, the completion dates for actions already taken, and the estimated dates for completion of planned actions. If you nonconcur, please state your specific reasons for each nonconcurrence. If appropriate, you may propose alternative methods for accomplishing desired improvements. Recommendations are subject to resolution in accordance with DoD Directive 7650.3 in the event of nonconcurrence or failure to comment.

The courtesies extended to the audit staff are appreciated. If you have any questions about this audit, please contact Mr. F. Jay Lane, Program Director, at (703) 693-0430 (DSN 223-0430), or Mr. Richard B. Bird, Project Manager, at (703) 693-0476 (DSN 223-0476). Appendix F lists the planned distribution of this report.

A handwritten signature in cursive script, reading "Robert J. Lieberman".

Robert J. Lieberman
Assistant Inspector General
for Auditing

Enclosures

cc:

Secretary of the Air Force
Assistant Secretary of the Air Force (Financial
Management and Comptroller)
Director, Defense Finance and Accounting Service
General Counsel, Department of Defense

Office of the Inspector General, DoD

AUDIT REPORT NO. 93-053
(Project No. 2FG-5001)

February 12, 1993

**AUDIT REPORT ON THE MISSILE PROCUREMENT
APPROPRIATIONS, AIR FORCE**

EXECUTIVE SUMMARY

Introduction. The Comptroller of the Department of Defense requested the audit because the Air Force had reported problems with funding upward adjustments to obligations for contract changes whose costs were chargeable to expired appropriations. Those changes were previously funded from the Air Force's merged ("M") accounts. The National Defense Authorization Act for Fiscal Year 1991 phased out merged accounts and made all appropriations available for disbursements and adjustments for 5 fiscal years following expiration. Agencies must maintain fiscal year appropriation integrity when creating obligations and paying bills.

Objectives. The objectives of the audit were to assess the extent of the potential deficiencies in the FYs 1987 and 1988 Missile Procurement Appropriations, Air Force (MPAAF), and the need for legislative relief to meet program commitments affected by the "M" account legislation of 1991.

Audit Results. The audit concluded that the FYs 1987 and 1988 Air Force missile procurement appropriations were deficient and that legislative relief was needed.

- o The Air Force accounting and budget decisions on the financing and reporting of contract growth caused finance and accounting records to be materially misstated. Violations of some of the Antideficiency Act provisions in the United States Code (U.S.C.) occurred; specifically, 31 U.S.C. secs. 1341 and 1502 were violated. However, the value of the deficiencies in the appropriations cannot be calculated until the impact of unapproved upward obligation adjustments is determined, funding issues and accounting problems are resolved, and contingent liabilities are fully reflected in the accounting records (**Finding A**).

- o To avoid declaring a violation of the Antideficiency Act, Air Force officials terminated contracts for the Advanced Cruise Missile for the convenience of the Government and initiated reprocurement action on the following day using FY 1992 funds. They did this because insufficient funds remained in the FYs 1987 and 1988 missile procurement appropriations to pay for work remaining to be performed on the original contracts. As a result of the contract terminations, the Air Force may have to assume \$24 million to \$49 million in additional costs that would have

been assumed by the contractor under the original contracts. Funding violations still occurred, because funds available for obligation were insufficient to correct deficiencies in the FYs 1987 and 1988 missile procurement appropriations (**Finding B**).

Legislation was needed in order to prevent the disruption of major DoD procurements when unrecorded obligations and obligational adjustments properly chargeable to prior year appropriations exceeded funds available for obligation in expired year accounts. We supported the legislation, proposed by the DoD Comptroller, that was incorporated with modifications into the National Defense Authorization Act for Fiscal Year 1993. This legislation will permit DoD to use current funds to pay obligations properly chargeable to expired accounts. (Similar authority presently exists in the "M" account legislation, which allows DoD agencies to pay from current funds the obligational adjustments otherwise chargeable to closed accounts.) The National Defense Authorization Act for Fiscal Year 1993 allows major programs to continue, but requires that funding violations be reported under the Antideficiency Act when current funds are used. The legislation also permits changes to acquisition, budgeting, and accounting practices.

Potential Benefits of Audit. Recommendations in this report, if implemented, will result in compliance with regulations and improved economy and efficiency of operations in appropriations management. Fiscal responsibility should improve when the Air Force corrects practices such as the underreporting of obligated amounts and delayed recording of obligations. We did not quantify any monetary benefits; Appendix D lists other potential benefits of our audit.

Summary of Recommendations. We recommended that the DoD Comptroller investigate and report the Antideficiency Act violations for the FYs 1987 and 1988 MPAAFs; direct the Air Force to use existing legislative authority to pay obligational adjustments chargeable to expired year accounts from current appropriations; and notify Congress that violations of the Antideficiency Act exist. We recommended that contracts be obligated at best-cost estimates instead of target level; that recorded obligations be revised as data become available; that these estimates be recorded as expired year requirements and recognized in "Reports on Budget Execution" (DD Forms 1176); and that budget activities promptly approve changes to expired year obligations. We also recommended that DoD accelerate plans to resolve negative unliquidated obligations by using the same records to account for funds and pay bills and by assuring that funds are available before making payments.

Management Comments. The Deputy Comptroller of the Department of Defense (Management Systems) concurred or partially concurred with all recommendations.

Although we did not make recommendations to the Air Force, we received comments from them. The Air Force agreed that the missile procurement appropriations for FYs 1987 and 1988 were deficient, but stated that the degree of deficiency had changed. Recognizing that the fiscal status of those appropriations is not static, we made no attempt to reconcile the new data provided by the Air Force, or to determine whether the Air Force had made proper funding decisions in adjusting its account balances. We disagree with the Air Force's conclusion that it was proper to terminate the Advanced Cruise Missile contracts and reprocure them with current year funds to avoid reporting Antideficiency Act violations in prior year accounts. See Part IV of this report for the text of the Deputy Comptroller and Air Force responses and Part II for our evaluation of the Deputy Comptroller's response.

Audit Response. Since Congress passed the National Defense Authorization Act for Fiscal Year 1993, which includes legislation proposed by the DoD Comptroller, we have revised Recommendation A.2. We are requesting that the DoD Comptroller direct the Air Force to use this legislative authority to use current appropriations to pay for the obligational adjustments that would otherwise be properly chargeable to expired appropriations except for the fact that there are no funds remaining in the expired appropriation, and to notify Congress of any violations of the Antideficiency Act. Although management agreed with the other recommendations, we do not consider the responses on several items to be adequate; therefore, we request that they be reconsidered or expanded. We have also deleted Recommendation A.8. which was designed to permit contingent liabilities (contractor incentives and award fees) to be funded with current year funds. The DoD Comptroller maintained that additional relief was not needed at this time. We plan to address this issue during a forthcoming audit of canceled unliquidated obligations.

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This report was prepared by the Financial Management Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate, (703) 614-6303 (DSN 223-6303).

PART I: INTRODUCTION

Background

The National Defense Authorization Act for Fiscal Year 1991, Public Law 101-510, November 5, 1990 (the Act), phased out merged accounts ("M" accounts). The law stated that after the end of the period of availability for obligation of a fixed appropriation account and before the closing of that account, the account shall retain its fiscal-year identity and remain available for recording, adjusting, and liquidating obligations properly chargeable to that account. After a 5-year period, accounts are closed, and any remaining balances (whether obligated or unobligated) are canceled and thereafter are not available for obligation or expenditure for any purpose. Therefore, obligations and adjustments to obligations that would have been properly chargeable to those accounts (both as to purpose and amount) before closing, and that are not otherwise properly chargeable to any current appropriation account, may be charged to any current appropriation account available for the same purpose. Beginning with FY 1987 appropriations, "M" accounts were no longer available to fund obligation adjustments. Appropriations must maintain their original fiscal-year identities when creating obligations and paying bills.

A contract that is in compliance with the Adequacy of Appropriations Act, 41 U.S.C. sec. 11, because sufficient funds were available when the contract was signed, can still result in a violation of the Antideficiency Act, 31 U.S.C. sec. 1341, if during the period before payment is due, the amount of the available appropriations becomes inadequate to pay contract obligations, obligational adjustments, and other liabilities.

A violation of 31 U.S.C. sec. 1341 occurs if obligations and obligational adjustments that would have been properly chargeable to an expired appropriation during the 5-year period of availability exceed the available balance of that appropriation. If this happens, deficiencies are normally met by a supplemental or deficiency appropriation or other Congressional action.

On December 10, 1990, the Comptroller of the Department of Defense (the DoD Comptroller) issued initial guidance to implement the Act. The guidance was revised and clarified twice. On June 13, 1991, the DoD Comptroller prescribed that current year appropriations be used to fund upward adjustments for contract changes and any other change(s) that result in additional contractor billable costs. On April 20, 1992, the DoD Comptroller issued revised guidance requiring that within-scope contract changes be funded with the appropriate expired year appropriations. The revised guidance stated that "the policy regarding the charging of contract changes shall be the same policy in effect prior to June 13, 1991," and that DoD

Components are to follow the provisions of Chapter 25 of the "DoD Accounting Manual" (DoD Manual 7220.9-M, June 6, 1988). The revised accounting policy reconfirmed that within-scope adjustments to prior year contracts must be obligated against available balances of the fiscal year appropriations which initially financed the original contract.

On April 6, 1992, Air Force officials formally advised the DoD Comptroller that they anticipated violations of the Antideficiency Act in several appropriations. The violations included deficiencies in the Missile Procurement Appropriation, Air Force (MPAAF) (appropriation symbol 57*3020), estimated at \$93.6 million for FY 1987 and \$89.2 million for FY 1988. On April 6, 1992, the Air Force was already taking action to terminate the unexecuted portion of the FY 1987 Advanced Cruise Missile (ACM) contract for the Government's convenience. On April 7, 1992, the Air Force issued a new letter contract to continue the terminated ACM work with FY 1992 MPAAF funds. On April 9, 1992, the Air Force partially terminated the FY 1988 ACM contract for the Government's convenience and funded residual requirements from the FY 1992 MPAAF.

On April 7, 1992, the DoD Comptroller requested that the Inspector General, DoD, review the FY 1987 MPAAF.

Objectives

The primary objective of the audit was to assess the extent of the potential deficiencies in FYs 1987 and 1988 for the MPAAF, and the need for legislative relief to meet program commitments affected by the "M" account legislation of 1991.

Scope

The DoD Comptroller requested this financial audit. We made the audit from April through May 1992. During the audit, we reviewed program managers' requests for upward obligation adjustments affecting the MPAAF appropriations for FYs 1987 and 1988. To assess reported budgetary needs, we interviewed MPAAF program managers at the Space Systems Division, Los Angeles, California; the Ballistic Missile Office, Norton Air Force Base (AFB), California; the Aeronautical Systems Division (Detachment 24), Eglin AFB, Florida; and the Aeronautical Systems Division, Wright-Patterson AFB, Ohio. At these locations and at Hill AFB, Utah, we reviewed accounting records to assess the accuracy of obligation data in DoD's "Report on Budget Execution," DD Form 1176, dated March 31, 1992. Appendix E lists the activities we visited or contacted.

Limitations. Our scope was limited because the DoD Comptroller asked us to make only an initial assessment of the appropriations' status and because we had a short time period in which to perform the work. We did not evaluate the validity of obligations already recorded in the Air Force finance and

accounting system, the reliability of computer-processed data, or the implementation of the Federal Managers' Financial Integrity Act. Except for the ACM contract, we made no attempt to identify obligations from FYs 1987 and 1988 that the Air Force may have paid with current year funds.

Auditing standards. The audit was made in accordance with auditing standards issued by the Comptroller of the United States as implemented by the Inspector General, DoD.

Prior Audits and Other Reviews

Both the General Accounting Office (GAO) and the Inspector General, DoD, have evaluated DoD's "M" accounts and related issues.

GAO reviews. The GAO issued two reports on related topics:

- o "Air Force Systems Command Is Unaware of the Status of Negative Unliquidated Obligations," GAO/AFMD 91-42, GAO Code 903114, was issued on August 29, 1991. The GAO observed that weaknesses existed in managing negative unliquidated obligations within the Air Force.

- o "Strategic Missiles: ACM Program, Opportunity for Additional Savings," GAO/NSIAD 92-154, GAO Code 392526, was issued on May 6, 1992. The GAO observed that shortfalls for funding the ACM were estimated at \$121 million. The GAO reported that when the Air Force determined that sufficient FYs 1987 and 1988 funds were not available, it partially terminated the ACM contract. According to the GAO, the Air Force then awarded a new letter contract to continue the work being done under the partially terminated contract, using funds that were appropriated in FY 1992. The GAO expressed concern about the Air Force's actions, citing the potential for cost increases and the legal and program issues that could arise. DoD generally agreed with the report's findings.

Inspector General, DoD. The Inspector General, DoD, recently issued three reports on "M" accounts and the Air Force's missile procurement appropriations:

- o "Merged Accounts of the Department of Defense," Report No. 92-028, issued on December 30, 1991, showed that obligations in DoD accounting records did not accurately reflect the status of accounts. The audit disclosed errors in Air Force records, including the MPAAF, and the auditors found that DoD's "M" accounts had about \$1 billion recorded as negative unliquidated obligations. The report noted that several of DoD's merged accounts, including the Air Force's, were overobligated or overexpended. The auditors expressed concern because official DoD accounting records were so inaccurate that the DoD Comptroller felt it was necessary to request restorations to cover unrecorded obligations that the Military Departments had

identified by other than official accounting records. The Deputy Comptroller (Management Systems) generally agreed with the report.

o "Titan IV Program," Report No. 92-064, issued on March 31, 1992, showed that progress payments for the Titan IV contract were made from a predetermined sequence of appropriations, rather than from appropriations that reflected the type of work done. The Commander, Defense Contract Management Command, and the Program Executive Officer nonconcurred with the recommendations in the report, pending review by the DoD Comptroller. The issues have not yet been resolved.

o Report No. 92-132, "Management of the Titan IV Solid Rocket Motor Upgrade Subcontract," issued September 2, 1992, concluded that the financing arrangement for the subcontract was not viable or equitable. The Department of Defense Appropriations Act, 1993, Public Law 102-396, sec. 9164, gave the Air Force authority to use FY 1992 or FY 1993 funds to fund a supplemental agreement to the Titan IV prime contract for the solid rocket motor upgrade.

We did not follow up on recommendations in previous reports because actions were being taken to correct the deficiencies.

PART II: FINDINGS AND RECOMMENDATIONS

A. ASSESSMENT OF THE AIR FORCE MISSILE PROCUREMENT APPROPRIATIONS FOR FYS 1987 AND 1988

The balances in the Air Force missile procurement appropriations for FYS 1987 and 1988 were insufficient to meet obligations and obligational adjustments properly chargeable to those appropriations. To pay for contract growth, Air Force officials made accounting and budget decisions that caused finance and accounting records to be materially misstated. Violations of the Antideficiency Act, 31 U.S.C. secs. 1341 and 1502, resulted. We estimate that as of March 31, 1992, the deficiencies were about \$119 million for FY 1987 and \$183 million for FY 1988. However, the exact value of the deficiencies cannot be fixed until the impact of unapproved upward obligational adjustments is determined, funding issues and accounting problems are resolved, and contingent liabilities are fully reflected in the Air Force's accounting records and "Report on Budget Execution."

DISCUSSION OF DETAILS

Background

Time limits on the availability of appropriations for obligation and expenditure are found in 31 U.S.C. sec. 1502(a), which states, "The balance of an appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability or to complete contracts properly made within that period of availability and obligated consistent with section 1501 of this title. However, the appropriation or fund is not available for expenditure for a period beyond the period otherwise authorized by law."

The National Defense Authorization Act for Fiscal Year 1991 also established a transition period to phase out "M" accounts. Section 1557 canceled all merged surplus authority effective on December 5, 1990; however, it also permitted a one-time restoration of unobligated amounts withdrawn under 31 U.S.C. sec. 1552(a)(2) to pay for obligations and adjustments to obligations. In the past, the surpluses had been available to Defense activities and were used to fund contract growth. At the time the "M" accounts were canceled, only \$18.6 million in unobligated funds remained in the Missile Procurement Appropriations, Air Force (MPAAF), account in the U.S. Treasury. The law also extended the expired status of existing appropriations from 2 to 5 years.

The DoD Comptroller recognized that in order to compensate for the unavailability of "M" account balances, alternate sources of legally available funds must be found to pay for adjustments properly chargeable to expired year appropriations. Additional funds were needed to avoid program interruptions and increased

costs, until acquisition and accounting practices could be changed. On April 30, 1992, the DoD Comptroller transmitted a supplemental appropriations request to the Director, Office of Management and Budget (OMB), proposing legislation to authorize current appropriations to pay obligations and obligational adjustments properly chargeable to expired accounts (see Appendix A). The request sought authority for fixed appropriations for FY 1992 and prior fiscal years. The proposed legislation would have allowed the use of current year funds that are for the same purpose as an expired account to pay obligations and adjustments to obligations that, if sufficient obligational authority existed, would have been chargeable to expired accounts. DoD Components would be required to report any violations of the Antideficiency Act that required use of this authority. We believe the DoD Comptroller was justified in requesting legislation to resolve funding shortfalls. Appendix A contains the text of the legislation proposed by the DoD Comptroller. Appendix B includes section 1004 of the National Defense Authorization Act for Fiscal Year 1993, which contains the authority as approved for fiscal years before 1992 and reaffirms the requirement to report Antideficiency Act violations.

Accounting and Budget Decisions Affecting the MPAAF

Deficiencies in FYs 1987 and 1988 Air Force Missile Procurement Appropriations. Our review of the Air Force appropriations showed that deficiencies existed in the MPAAFs for FYs 1987 and 1988; that obligations were not promptly recorded in official accounting records; and that the Air Force violated the Antideficiency Act. Our review showed the following deficiencies as of March 31, 1992, in Air Force appropriations.

FYS 1987 AND 1988 DEFICIENCIES IN AIR FORCE MISSILE PROCUREMENT APPROPRIATIONS (\$ in millions)

<u>Deficiencies</u>	<u>FY 1987</u>	<u>FY 1988</u>
Unapproved upward obligation adjustments	\$ 30.7	\$ 72.0
Funding issues	113.4	113.4
Contingent liabilities	.0	32.1
 Subtotals	 <u>\$144.1</u>	 <u>\$217.5</u>
 Less available funds (as shown in "Reports on Budget Execution")	 <u>25.2</u>	 <u>34.5</u>
 Potential Deficiency	 <u>\$118.9</u>	 <u>\$183.0</u>

In addition to the deficiencies noted above, uncorrected accounting errors contributed to additional deficiencies in the MPAAFs (see section on "Negative Unliquidated Obligations"). These accounting errors totaled \$125.2 million for FY 1987 and \$160.6 million for FY 1988. Because of the accounting errors, the total deficiencies in the MPAAFs could be much larger.

Unapproved upward obligation adjustments. Upward obligation adjustments were not promptly approved and recorded as obligations. We also identified several accounting deobligation and budget adjustments that would affect the availability of funds and the Air Force's authority to approve upward obligation adjustments. The unrecorded adjustments discussed in the tables below, "Unrecorded Upward Adjustments" and "Unrecorded Deobligations," totaled \$30.7 million for FY 1987 and \$72 million for FY 1988.

Air Force requests to record upward obligation adjustments of \$100,000 or more must be approved by the Deputy Assistant Secretary of the Air Force (Budget). Our review showed that upward obligational adjustments were not approved to be placed on Air Force accounting records for long periods after the requests were submitted. For example, in February 1991, the Space Systems Division requested \$21.4 million in FY 1987 adjustments and \$24.4 million in FY 1988 adjustments for cost overruns in the Titan IV programs. As of April 7, 1992, the request had not been approved or recorded as an obligation.

Air Force budget officials stated that the delay in approving obligation adjustments resulted partly from the memorandum issued on June 13, 1991, by the DoD Comptroller, entitled "Revised DoD Guidance on Accounting for Expired Accounts, Including "M" and Merged Surplus Accounts." The guidance was interpreted to mean that contract changes had to be paid with current year funds. Air Force personnel stated that, although they complied with this DoD guidance, they were reluctant to do so. We believe that the Air Force also delayed the approval of obligation adjustments for expired year MPAAFs because insufficient expired year funds from FYs 1987 and 1988 were available to meet program requirements. In any event, the adjustments were not booked timely in either the expired or current year MPAAF accounts.

Unrecorded upward adjustments. During discussions with project managers, we verified that a number of upward obligation adjustments were awaiting approval by the Secretary of the Air Force (Air Staff) before being recorded in official accounting records. As of April 7, 1992, there were about \$31 million (FY 1987) and \$83.5 million (FY 1988) in unreported upward adjustments. These totals included \$20.5 million in additional unreported upward adjustments to the MPAAF, all identified by us.

UNRECORDED UPWARD ADJUSTMENTS

<u>Unrecorded Upward Adjustments</u>	<u>FY 1987</u>	<u>FY 1988</u>
Titan IV adjustments	\$21,100,000	\$24,400,000
Forward pricing adjustment		7,363,000*
Peacekeeper	0	9,000,000*
Advanced Medium Range Air-to-Air Missile (AMRAAM)		
Lot I	8,460,000	0
Lot II	0	36,200,000
AMRAAM predictability program	490,000	4,210,000
Air Intercept Missile-9	730,000	396,000
Plant 44	247,000	0
Tacit Rainbow award fee	0	61,000*
Advanced Cruise Missile award fee	<u>0</u>	<u>4,100,000*</u>
Total unrecorded budget adjustments	<u>\$31,027,000</u>	<u>\$83,530,000</u>

*Adjustments identified by IG, DoD.

Unreported deobligations. We also identified unreported accounting adjustments that would offset some of the financial pressure on the expired MPAAF accounts. Program officials did not want to report identified deobligations to higher headquarters, because they believed the funds would be withdrawn and reprogrammed. For example, contracting officials stated that \$8.7 million in Tacit Rainbow funds would probably be deobligated during the fourth quarter of FY 1992. However, this information was not reported to the Air Staff. The following table shows the unreported accounting deobligations that we identified. Failure to identify and report deobligations as promptly as possible distorts the available balances of the appropriations and reduces management's decisionmaking ability.

UNREPORTED DEOBLIGATIONS

<u>Deobligations</u>	<u>FY 1987</u>	<u>FY 1988</u>
Rapier accounting error	\$ 0	\$ (3,700,000)
Plant 44 Deobligations	(313,000)	(200,000)
Tacit Rainbow deobligations	0	(8,700,000)
AMRAMM Contract Adjustment	<u>0</u>	<u>(1,100,000)*</u>
Total	<u>\$(313,000)</u>	<u>\$(13,700,000)</u>

*Adjustment identified by IG, DoD.

Funding issues. Although Air Force officials stated that they were reluctant to use current year funds for certain within-scope prior year contract adjustments, the Air Force did plan to use current or future year funds for several prior year requirements.

In addition to obligations properly chargeable to expired year funds that had not been recorded, field activities incorrectly approved, or were forwarding for approval, the following funding requests for current and future year dollars.

FYS 1987 AND 1988 OBLIGATIONS FUNDED WITH FY 1992 AND FUTURE YEAR DOLLARS (\$ in millions)

<u>Program</u>	<u>FY 1987</u>	<u>FY 1988</u>
Advanced Cruise Missile	\$111.5	\$54.7
Titan IV	0	46.7
Titan II	1.9	2.0
Advanced Medium-Range Air-to-Air Missile	<u>0</u>	<u>10.0</u>
Total obligations funded with 1992 and future year dollars	<u>\$113.4</u>	<u>\$113.4</u>

Advanced Cruise Missile (ACM) recapitulation. To avoid reporting potential violations of the Antideficiency Act in the Air Force missile procurement accounts, the Air Force terminated portions of the FYs 1987 and 1988 ACM contracts and immediately recapitulated the unexecuted portions. Therefore, within-scope upward adjustments of \$111.5 million from FY 1987 and \$54.7 million from FY 1988 were inappropriately funded with FY 1992 dollars. See Finding B for a detailed discussion of the ACM recapitulation.

Titan IV stretch-out. The Air Force has deferred scheduled launches of satellites from the Titan IV missile, and production of the Titan IV has been extended. Air Force officials stated that they planned to use FY 1992 funds to pay \$15.1 million of the \$46.7 million in cost growth for the remaining unlaunched Titan IV missiles from FY 1988. We were later told that this estimate may decrease because one or more of the FY 1988 missiles may have been completed. Based on the cost of the undelivered missiles, we estimated that out of the \$46.7 million in FY 1992 and future year adjustments, as much as \$31.6 million should also be charged to the FY 1988 MPAAF for storage and sustaining engineering costs. The FYs 1987 and 1988 share of the delayed Titan IV costs should be funded from the expired year appropriation accounts to the extent that balances are available, and a deficiency or supplemental appropriation should be sought if they are not. We believe the incremental funding authority in the Department of Defense Appropriations Act, 1993, Public Law 102-396, sec. 9164, does not apply retroactively to obligations and adjustments properly chargeable to the expired year accounts.

Titan IV program managers plan to charge \$116 million to FY 1992 and future years to pay for storage and engineering costs incurred when production of the missile was postponed. Air Force officials were attempting to shift cost increases between fiscal years by asking classified and unclassified users to trade missiles; however, these efforts had not been successful. These charges should be funded with FY 1988 expired year funds to the extent that those funds are available; an Antideficiency Act violation is reportable to the extent that they are not.

Titan II overruns. Program managers said they had requested FY 1990 funds to pay for cost overruns of \$1.9 million for FY 1987 and \$2 million for FY 1988. The request was pending at the time of our audit. The requirements represent a target-to-ceiling contract liability; the Government is liable for 90 percent of these amounts, and the contractor is liable for 10 percent of the additional engineering work performed by the contractor. Although the requirements still exist, the overruns remain unfunded and should be funded with FYs 1987 and 1988 funds to the extent that those funds are available, further increasing the deficiency to the extent that they are not.

Erroneous specifications in Lot II of the Advanced Medium Range Air-to-Air Missile (AMRAAM). In November 1991, program managers requested authority to use FY 1988 funds for a \$10 million upward adjustment for the AMRAAM. However, we were told that Air Force budget personnel now plan to use FY 1992 funds to pay for this adjustment. The \$10 million adjustment would pay a negotiated settlement of \$8 million to \$24 million under the FY 1988 contract. The settlement was negotiated because the Air Force had included defective specifications in the F-15 aircraft contract. The Air Force should use FY 1988 funds to pay for this adjustment to the extent that funds are

available, which will increase the deficiency in the MPAAF to the extent that they are not.

Outdated accounting practices. Chapter 25 of the "DoD Accounting Manual," DoD Manual 7220.9-M, requires that DoD Components budget against a target amount for major procurements, even though the ceiling price may be higher. Therefore, the Air Force has been obligating funds against a target level, instead of a ceiling or a higher best estimate, and has not adjusted the obligated amounts when the actual costs become known. Before the enactment of Public Law 101-510 and the National Defense Authorization Act for Fiscal Year 1991, merged account funds were available, and budgeting for contracts at target levels was a common practice. However, these funds are no longer available to pay for contract growth after appropriations expire. Instead, funds are now available for 5 years after an appropriation expires, instead of an indefinite period, as under the old system when the accounts merged. For these reasons, obligating funds for major procurements at target cost levels is fiscally unwise.

Air Force officials agreed that they must change their procurement, acquisition, and funding practices. However, some Air Force and DoD officials maintained that it would be unwise to budget for higher than the original target costs; they said this would send an undesired message to contractors that cost growth beyond the target level (the original negotiated contract price) was acceptable. The Air Force must recognize that obligations for major procurements have a history of sizable growth. Upward adjustments to contracts must also be promptly approved or disapproved. The failure to realistically assess contract growth from beginning to end of a procurement could result in a violation of the Antideficiency Act.

Contingent liabilities. A contingent liability represents a potential Government obligation. Government accounting policy requires contingent liabilities to be recorded as obligations only when the event occurs. However, unrecorded contingencies can greatly increase the need for expired year funds. The MPAAF had at least \$32.1 million in contingent liabilities that should be paid with FY 1988 funds. Contingent liabilities for contracts from expired years (FYs 1987 and 1988) for incentives and award fees must be obligated against funds from the fiscal year against which the original contract was funded. Upon cancellation of those appropriations, any contingent liability must be funded from current year dollars. In the past, DoD funded these requirements with merged year dollars.

Awards and incentives. Paying contractor awards and incentives could require the outlay of additional MPAAF funds, which could further increase the deficiency. We identified \$32.1 million in contingent liabilities from FY 1988. This amount represents awards and incentives that the Air Force plans to fund with appropriations that are current when the bills are

presented to the Government for payment. These obligations include "mission success fees" of \$21.6 million for Titan IV and \$10.5 million for Titan II. Titan program officials maintained that the incentives should be paid from FY 1992 funds and that FY 1992 contracts have been structured to provide this funding. Current fiscal standards for recording commitments and obligations under existing law provide that obligations for award fees and incentive fees must be recorded against the same source of funds that was originally obligated for the contract. (See DoD 7220.9-M, Chapter 25, paragraph 11.)

Other accounting issues. The DoD "Report on Budget Execution," DD Form 1176, gives financial data and shows the monthly status of each DoD appropriation; managers make major funding decisions based on that report. However, the report does not give managers all the information they need about the availability of expired year funds.

Commitments. Expired year commitments are funds that are administratively reserved for future use but not obligated. The "Report on Budget Execution" does not count commitments for expired year appropriations against the money that is available to fund upward adjustments. We found that Air Force accounting activities were inconsistent in reporting commitments. In the "commitments" category, some accounting activities reported upward adjustments that they planned to pay with expired year funds; other activities reported the same types of transactions as obligations that would count against expired year appropriations available to fund upward adjustments. Because of the inconsistency in reporting commitments, managers could erroneously approve payment of upward adjustments with expired year funds, which could increase the MPAAF deficiency.

Negative unliquidated obligations. Negative unliquidated obligations (NULOs) are errors (except for progress payments and refunds) that occur when a disbursing station makes a payment against a contract for which the accounting station's records show that money is either insufficient or unavailable. NULOs can significantly decrease the available balance of an appropriation, as shown in "Reports on Budget Execution." MPAAF records showed \$125.2 million in NULOs in FY 1987 and \$160.6 million in NULOs in FY 1988. As of March 31, 1992, the following NULO balances (excluding progress payments and refunds) existed at the audit locations we visited.

**NEGATIVE UNLIQUIDATED OBLIGATIONS IN THE
MISSILE PROCUREMENT APPROPRIATIONS, AIR FORCE**
(\$ in millions)

<u>Audit Location</u>	<u>FY 1987</u>	<u>FY 1988</u>
Los Angeles AFB, CA	\$ 93.8	\$158.1
Wright-Patterson AFB, OH	15.9	1.0
Norton AFB, CA	1.0	.9
Eglin AFB, FL	14.0	.2
Hill AFB, UT	<u>.5</u>	<u>.4</u>
Totals	<u>\$125.2</u>	<u>\$160.6</u>

NULOs must be recorded in the accounting records and researched to identify and correct errors such as the fiscal year, contract, contract line, appropriation, or agency. However, NULOs may also represent overpayments to vendors that must be reconciled. Unresolved NULOs can cause the true amount of unobligated funds to be misrepresented in "Reports on Budget Execution," and can result in incorrect funding decisions and deficiencies in appropriations.

Space Systems Division, Los Angeles. Because of accounting practices at the Space Systems Division, Los Angeles AFB, it was impossible to determine the extent of the MPAAF deficiency. The Space Systems Division is responsible for most unclassified MPAAF funds. As of May 31, 1992, data at the Defense Finance and Accounting Service (DFAS), Denver Center, showed that the Space Systems Division had 370 contracts, from all appropriations and years, with net NULO balances of more than \$133 million. A contract has a net NULO balance when accounting lines with negative obligation values exceed lines with positive obligation values, excluding refunds, advances, and progress payments. A net NULO balance can be caused by an accounting error or a lack of funds to cover unpaid obligations. When obligated balances exceed available funds, a violation of the Antideficiency Act (31 U.S.C. sec. 1341) occurs. At the Space Systems Division, there is also a 3- to 6-month delay in recording expenditures made by disbursing stations at other locations, and discrepancies in accounting reports have not been reconciled. While no short-term solution is available, consolidating the base-level accounting and finance activities under DFAS may eventually improve accounting accuracy. However, at present, the Space Systems Division's records of expired and "M" year accounts are not a reliable basis for financial decisionmaking. Decisions based on these accounting records may be incorrect, and could result in appropriation deficiencies.

Conclusions

The balances shown in the official Air Force accounting records were materially misstated, and the balances in the Air Force

missile procurement appropriations for FYs 1987 and 1988 were insufficient to meet obligations and adjustments properly chargeable to those accounts. This violated the Antideficiency Act. Obligations and adjustments properly chargeable to these appropriations exceeded legally available balances. This occurred for various reasons, including the improper recording of obligations and the Air Force's widespread use of questionable funding practices. DoD officials incorrectly believed that sufficient merged account surpluses were still available in the Air Force missile procurement appropriations to avoid the deficiencies. After appropriations were closed and final restorations were made, less than \$18.6 million in unobligated funds remained in the MPAAF "M" year appropriations in the U.S. Treasury. Those unobligated funds would not have met the funding shortfalls for obligations and obligational adjustments properly chargeable to the FYs 1987 or 1988 accounts.

We supported the legislation proposed by the DoD Comptroller that was incorporated with modifications into the National Defense Authorization Act for Fiscal Year 1993. Section 1004 of the Act allows obligations and obligational adjustments that were properly chargeable to expired accounts to be paid from current year appropriations available for the same purpose. The legislation will prevent cost increases caused by canceling procurements and reprocurring items later at higher cost; will allow major congressionally-approved procurement programs to continue; and will leave reporting requirements of the Antideficiency Act intact. The legislation should give DoD adequate time to change its acquisition, budgeting, and accounting practices.

RECOMMENDATIONS FOR CORRECTIVE ACTION

We recommend that the Comptroller of the Department of Defense:

1. Investigate the Air Force violation of the Antideficiency Act, fix responsibility, and comply with the reporting requirements of DoD Directive 7200.1.

2. Direct the Air Force to use existing legislative authority to pay obligations and obligational adjustments properly chargeable to expired year accounts from current appropriations available for the same purpose, and notify Congress of any violations of the Antideficiency Act.

3. Require budget activities to report and promptly process upward obligation adjustments properly chargeable to expired year appropriations when these adjustments have been approved and are within the scope of the contract.

4. Direct the Air Force to fund within-scope obligation adjustments from expired years for the Advanced Cruise Missile, Titan IV, and the Advanced Medium-Range Air-to-Air Missile from

expired appropriations (to the extent that those funds are available).

5. Direct that all approved upward obligation adjustments from expired years (commitments or obligations) be included in "Reports on Budget Execution" (DD Forms 1176) to ensure full visibility of expired year financial activity.

6. Accelerate plans to solve problems with negative unliquidated obligations. At a minimum, these plans should require that a single record be used to account for funds and pay bills, and should require the disbursing station to ensure that funds are available before payment is made.

7. Revise DoD accounting policy to allow program managers to rely on best-cost to ceiling estimates and to adjust these obligations as more data become available.

8. In the draft report, we recommended that the DoD Comptroller seek legislation to allow contingent liabilities (contractor incentives and award fees) that remain as unliquidated obligations when the appropriation against which they were obligated is canceled, to be funded from the missile procurement appropriation that is current when the contractor earns the fees. This recommendation has been deleted from our final report; see below for management comments and audit response.

MANAGEMENT COMMENTS

We requested comments from the Comptroller of the Department of Defense (the DoD Comptroller) and received comments from the Deputy Comptroller (Management Systems) (the Deputy Comptroller). The Deputy Comptroller generally or partially concurred with all findings and recommendations in this report. The Air Force Deputy for Budget also commented.

In response to Recommendation A.1., the DoD Comptroller issued a memorandum, dated July 15, 1992, requesting that the Air Force investigate potential violations of the Antideficiency Act and that DFAS monitor the investigations closely.

Management's response to Recommendation A.2. stated that the DoD Comptroller had requested legislation that would authorize the use of current appropriations to pay obligations and adjustments properly chargeable to expired appropriations. This legislation was incorporated into Section 1004 of the National Defense Authorization Act for Fiscal Year 1993. The legislation also required the Secretary of Defense to certify to Congress that DoD Components are promptly submitting reports of violations of 31 U.S.C. sec. 1341, with all relevant facts and a statement of actions taken.

Management's response to Recommendation A.3. agreed that budget activities should be required to report and promptly process upward obligational adjustments chargeable to expired appropriations when these adjustments have been approved and are within the scope of the contract. The Deputy Comptroller stated that this is required by the "DoD Accounting Manual," DoD Manual 7220.9-M, Section B, Chapter 93. The Air Force comments stated that guidance would be issued to the field, reemphasizing the requirement to post obligations promptly once they have been recognized and approved.

Management partially concurred with Recommendation A.4. The Deputy Comptroller agreed that the Air Force should fund within-scope obligation adjustments associated with target-to-ceiling increases from expired year accounts. However, he maintained that consistent with DoD guidance current at that time, within-scope contract changes involving additional work should be funded from [then] current appropriations if the changes were approved between June 13, 1991, and April 19, 1992.

On Recommendation A.5., management agreed that all approved obligation adjustments chargeable to expired appropriations (commitments or obligations) should be included in the "Reports of Budget Execution" to ensure full visibility of expired year financial activity. The Deputy Comptroller stated that this is required by the "DoD Accounting Manual," Section B, Chapter 93.

On Recommendation A.6., management agreed that problems with negative unliquidated obligations must be solved. The Deputy Comptroller doubts that using one record to both account for and pay obligations can be done immediately. Nevertheless, he has requested that DFAS take all possible actions to reduce undistributed disbursements and eliminate negative disbursements. He also stated that DoD has established a Joint Contract Accounting and Finance Process Review Group to develop short-term, cost-effective solutions and propose policy changes.

On Recommendation A.7., the Deputy Comptroller stated that when obligations are recorded on fixed-price incentive contracts, target prices represent best-cost estimates at the time a contract is awarded. After DoD signs a contract, if the best-cost estimate varies from the initial target price, obligations should be adjusted. He directed that the "DoD Accounting Manual," Section B, Chapter 25, Paragraph D.2., be revised, and that the following paragraph be included in DoD Regulation 7000.14-R, "DoD Financial Management Regulation," by March 31, 1993:

2. Fixed-Price Contract with an Escalation, Price Redetermination, or an Incentive Provision. When a contract is awarded, an obligation must be recorded for the amount of the target or billing price stated in the contract, even though the contract may

contain a ceiling price in a larger amount. Subsequently, a target or billing price should be adjusted upward or downward to a "best-cost estimate" whenever it is determined that, and documentary evidence supports, the actual cost of the contract will differ materially from the original target or ceiling price stated in the contract.

On Recommendation A.8., management stated that DoD's policy is to cover contingent liabilities, such as incentive and award fees, within the amounts authorized by Congress. The Deputy Comptroller stated that limited relief has been provided in the National Defense Authorization Acts for Fiscal Years 1991 and 1993. This legislation gives DoD sufficient authority to charge contingent liabilities to current appropriations when sufficient funds are not available in merged or expired accounts. He stated that additional legislation is not needed at this time.

The complete text of management's comments is in Part IV.

AUDIT RESPONSE

The "Response Requirements on Recommendations" chart at the end of this section lists the requirements for further comments.

The Deputy Comptroller concurred with Recommendation A.1. and has requested that the Air Force investigate potential Antideficiency Act violations and that DFAS closely monitor the progress of these investigations. This response fulfills the intent of our Recommendation A.1.

The Deputy Comptroller's actions were responsive to Recommendation A.2. as originally written. The DoD Comptroller submitted a request for legislative relief, which was approved by Congress. The National Defense Authorization Act for Fiscal Year 1993 gives DoD the authority to use current appropriations to pay obligations and adjustments properly chargeable to expired appropriations. The Act also requires the Secretary of Defense to report antideficiency violations to Congress immediately, with all relevant facts and a statement of actions taken. We have revised Recommendation A.2.; we are requesting that the DoD Comptroller direct the Air Force to use the revised legislative authority to fund obligations or obligational adjustments otherwise properly chargeable to expired appropriations when there are insufficient funds in the expired appropriations. We request that the DoD Comptroller provide comments on the revised recommendation.

Management concurred with Recommendation A.3., stating that the "DoD Accounting Manual" already gives procedures for prompt processing of upward obligation adjustments. The intent of the

recommendation will be met when Air Force field activities are reminded of the requirement to post obligations promptly once they are recognized and approved.

Management partially concurred with Recommendation A.4., stating that within-scope adjustments associated with target-to-ceiling increases should be funded from expired accounts. The Deputy Comptroller exempted those changes approved between June 13, 1991, and April 19, 1992, which involved the use of current year appropriations. The DoD guidance that was operative during that period was contrary to the law. It was subsequently reversed. We believe that all improper charges made as a result of that guidance should be reversed and should be charged to expired appropriation accounts, to the extent that sufficient balances remain in those accounts to cover the obligations. When sufficient funds are not available, current year funds should be used, and a violation of the Antideficiency Act should be reported to Congress. We request that the DoD Comptroller reconsider the initial response.

Management concurred with Recommendation A.5., citing the "DoD Accounting Manual," Section B, Chapter 93. However, the Deputy Comptroller's comments are nonresponsive. The "DoD Accounting Manual," Section B.8.c.(27), Chapter 93, prohibits the recording of commitments for expired year accounts. OMB Bulletin No. 93-02 requires that funded and unfunded liabilities, including both commitments and contingencies, be included in agencies' financial statements. Unless managers know the amounts that have been committed (as much as several million dollars), improper financial decisions may be made. We request that the DoD Comptroller reconsider the initial comments and provide revised comments on Recommendation A.5. in this final report. The comments should contain a plan for modifying procedures to require that both commitments and obligations be shown on DD Form 1176, "Report of Budget Execution," for expired year appropriations.

Management concurred with Recommendation A.6. We acknowledge the problems and expenses in establishing a single record to account for funds and pay bills, and we consider the Deputy Comptroller's comments to be responsive. However, we request that the DoD Comptroller provide an action plan with specific milestones to ensure that this effort receives a high priority.

The Deputy Comptroller partially concurred with Recommendation A.7. We consider his comments to be responsive, and no further action is required.

The Deputy Comptroller partially concurred with Recommendation A.8., stating that at this time, there is no need for additional legislation to permit award fees to be paid from funds that are current when the fee is earned. He believed that the revised legislation gave DoD sufficient funds to meet liabilities. We have deleted this recommendation; however, our review showed that

the Air Force is experiencing difficulty in managing contingencies for incentives and awards, and may be forced to declare a number of Antideficiency Act violations. The National Defense Authorization Act for Fiscal Year 1991 and the National Defense Authorization Act for Fiscal Year 1993 provide limited relief; section 1004 of the latter Act applies only in the case of an appropriation account for a fiscal year prior to FY 1992. Incentive and award fees that are recorded as obligations against appropriations that funded the original contract, but that remain unliquidated when the appropriation is canceled, must be liquidated using current year funds. We plan to address this issue during a forthcoming audit.

RESPONSE REQUIREMENTS ON RECOMMENDATIONS

Responses to the final report are required from the Comptroller of the Department of Defense for the items indicated with an "X" in the chart below.

<u>Recommendation Number</u>	<u>Response Should Cover:</u>		
	<u>Concur/ Nonconcur</u>	<u>Proposed Action</u>	<u>Completion Date</u>
A.2.	X	X	X
A.4.	X	X	X
A.5.		X	X
A.6.		X	X

B. REPROCUREMENT OF THE ADVANCED CRUISE MISSILE

To avoid declaring a violation of the Antideficiency Act, Air Force officials terminated contracts for the Advanced Cruise Missile (ACM) and initiated reprocurement actions the following day using current year funds. They did this because insufficient funds were available in the FYs 1987 and 1988 MPAAF. Because of the Air Force's actions, the Government may have to assume an additional \$24 million to \$49 million in contractor liabilities. Furthermore, the Air Force's actions did not prevent a violation of the Antideficiency Act.

DISCUSSION OF DETAILS

Background

The Air Force was short of funds for the FYs 1987 and 1988 ACM contracts. These shortages resulted partly from problems in missile production that required engineering changes. Only \$24.2 million remained in the FY 1987 MPAAF, and \$31.1 million in the FY 1988 MPAAF, to cover unpaid cost overruns. Therefore, on March 25, 1992, the Secretary of the Air Force approved a plan to terminate the ACM procurements at 520 missiles and finance the \$121 million in cost overruns with FY 1992 funds. On March 31, 1992, the DoD Comptroller denied the Air Force's request to use FY 1992 funds to cover cost overruns. The Air Force then chose another option, discussed below, to pay these costs.

Air Force ACM Procurement Actions

Three options considered. In July 1991, Air Force program officials determined that the cost of the FYs 1987 and 1988 ACM contracts would exceed budgeted targets and would approach or exceed ceiling costs. They also learned that the Air Force's FYs 1987 and 1988 MPAAFs did not contain enough funds to cover these adjustments. Air Staff officials were aware of the shortage, which was reported in the Defense Acquisition Executive Summary for August 1991 but was not resolved. Air Force officials considered three options:

- o to declare an Antideficiency Act violation in the MPAAF, notify Congress of the MPAAF shortages, and either request a supplemental appropriation or include the ACM requirements in the next budget submission;

- o to initiate a "stop work order" before depleting budgeted funds, and reprogram funds from other projects or fiscal years to pay for obligations on the ACM; or

- o to partially terminate the FYs 1987 and 1988 ACM contracts, reprocure the unexecuted portions with FY 1992 funds, and not report an Antideficiency Act violation.

The third option was selected, and in March 1992, the Assistant Secretary of the Air Force (Financial Management and Comptroller), with the concurrence of the Assistant Secretary of the Air Force (Acquisition), approved the use of FY 1992 funds to meet requirements that could amount to \$111.5 million from FY 1987 and \$54.7 million from FY 1988. The Air Force then partially terminated the ACM contracts and used FY 1992 funds to reprocure the remainder of the ACM requirements. Senior Air Force officials gave the following reasons for their actions.

- o Chapter 25 of the "DoD Accounting Manual" required budgeting to target when funding major procurements.

- o No requirement existed to record upward adjustments as obligations until they were incurred.

- o It was legal to cancel a contract one day, create a new contract the next day, and fund FYs 1987 and 1988 requirements with FY 1992 dollars, although the prior year contracts had been terminated to avoid Antideficiency Act violations in prior year accounts.

- o The Antideficiency Act had not been violated, since contractual obligations had not been recorded or executed.

- o Their actions prevented additional costs from being incurred on the FYs 1987 and 1988 contracts, for which expired year funds were not available; minimized the costs of terminating contracts; and sustained current production to meet operational requirements.

In April 1992, the Air Force informed Congress of the decision to terminate and reprocure the FYs 1987 and 1988 requirements for the ACM, and provided Congress with a closeout plan explaining the actions taken (see Appendix C).

Potential for increased liability. In our opinion, the Air Force's procurement actions were improper because the cost growth on the ACM contract did not result from out-of-scope changes or new work. The costs of within-scope changes and cost growth not related to new work were properly chargeable only to FYs 1987 and 1988 funds. Because of the new ACM contracts, the Air Force may have to pay an additional \$49 million in contract termination costs and liabilities that would have been absorbed by the contractor under the original contracts. The following table shows the additional reprocurement costs that the Air Force may have to pay.

ACM REPROCUREMENT LIABILITY
(\$ in millions)

<u>Liability</u>	<u>FY 1987</u>	<u>FY 1988</u>
Target-to-ceiling cost	\$20.0	\$24.0
Termination cost	<u>5.0</u>	<u>0</u>
Total liabilities	<u>\$25.0</u>	<u>\$24.0</u>

Funding deficiencies. The Air Force's use of FY 1992 funds to fund obligations and obligational adjustments properly chargeable to the MPAAFs for FYs 1987 and 1988, and its delay in recording the obligations, did not relieve the Air Force of its responsibility to investigate and report violations of the Antideficiency Act. In August 1991, Air Force officials recognized that the ACM program had funding problems; however, they said that they did not ask Congress for a supplemental appropriation because the June 13, 1991, guidance from the DoD Comptroller required the use of current year funds in such cases.

Disclosure to Congress. The Air Force also did not specifically disclose to Congress the increased costs that may have been incurred by terminating and reprocuring ACM requirements. In addition to incurring termination costs and penalties, the Government will have to pay the contractor's share (30 percent) of the liability for cost growth over target. Although program officials said that the contractor would not be allowed to use the new contract to recoup previous losses, the increased costs are estimated at \$24 million to \$49 million. Officials said that the contractor will absorb \$25 million in FY 1987 liabilities; however, they expect at least a \$24 million loss to the Government. Based on the closeout plan that the Air Force provided to Congress (Appendix C), we computed that the Government's liabilities resulting from contract termination could total \$79.7 million. However, neither this figure nor the estimated liability of \$24 million to \$49 million was included in the plan. The full impact of the Air Force's actions cannot be determined until the new letter contracts are definitized. After contracts were terminated, Congress rescinded the FY 1992 MPAAF funds that the Air Force intended to use for the reprocurement. As a result, the Air Force has incurred additional costs by entering into a new procurement, and must use another source of funds for the new ACM contracts.

Conclusion

The Air Force breached its fiduciary responsibility by incurring additional costs in an attempt to avoid reporting a violation of the Antideficiency Act. The decision of the Assistant Secretary of the Air Force (Financial Management and Comptroller) to finance a plan that would terminate parts of the FYs 1987 and

1988 ACM contracts and reprocure with new contracts was fiscally imprudent. We believe that the termination for convenience and the reprocurement will cost an additional \$24 million to \$49 million and do not relieve the Air Force of its responsibility to report a violation of the Antideficiency Act. Since Congress rescinded the FY 1992 funds that the Air Force planned to use for this reprocurement, the Air Force must find a legally available source of funds for the new contracts. Termination and reprocurement costs must also be charged to a supplemental appropriation unless sufficient funds remain in the original appropriations to cover these costs, because these costs are not chargeable to current appropriation accounts. The full impact of the Air Force's actions will not be known until the new contracts are definitized and Congress determines the number of missiles to be purchased. The Air Force tried unsuccessfully to use FY 1992 funds to pay for cost increases in the ACM because FYs 1987 and 1988 funds were insufficient. The Antideficiency Act was violated when the Air Force recognized that the cost to complete the ACM had exceeded amounts available for obligations, but permitted work to continue. Deficiencies in the FYs 1987 and 1988 MPAAFs are unresolved, the Antideficiency Act has been violated, and the Air Force has incurred additional costs by not reporting Antideficiency Act violations and requesting Congressional relief.

RECOMMENDATIONS FOR CORRECTIVE ACTION

See Finding A for our recommendations to correct problems with the procurement and funding of the ACM. Actions to correct the problems noted in this finding will be the same as actions for Finding A.

PART III: ADDITIONAL INFORMATION

- Appendix A: Legislation Proposed by the Comptroller of the Department of Defense
- Appendix B: Approved Legislation, National Defense Authorization Act for Fiscal Year 1993
- Appendix C: Advanced Cruise Missile Program Closeout Plan
- Appendix D: Summary of Potential Benefits Resulting from Audit
- Appendix E: Activities Visited or Contacted
- Appendix F: Report Distribution

**APPENDIX A: LEGISLATION PROPOSED BY THE COMPTROLLER OF THE DEPARTMENT
OF DEFENSE**



COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON, DC 20301-1100

APR 30 1992

**Honorable Richard G. Darman
Director
Office of Management and Budget
Old Executive Office Building
Washington, D.C. 20503**

Dear Mr. Darman:

On behalf of the Secretary of Defense, I am transmitting a supplemental appropriations request for the Department that redresses shortages of obligation authority in expired accounts and separately will provide additional transfers of \$429 million from the Defense Cooperation Account to the Army and Navy military personnel appropriations for increased incremental costs of Operation Desert Shield/Desert Storm.

The supplemental language regarding the expired accounts would authorize use of current appropriations for obligations and adjustments for prior year programs. This authority would permit the Department to pay obligations of expired accounts from current accounts similar to the authority that presently exists in Public Law 101-510 to pay obligations for closed accounts from current accounts after five years beyond expiration.

The new transfer authority requested for the military personnel appropriations is required to meet increased incremental Desert Shield/Desert Storm costs resulting from revised estimates of the active duty stop/loss effect and a greater number of reservists on active duty with longer tours than originally estimated. In addition the costs of imminent danger and family separation allowance payments have been greater than previously budgeted.

Proposed language for the supplemental request and supporting rationale are enclosed. The proposed rescissions which have been transmitted to Congress fully offset the fiscal year 1992 outlay estimate of this proposal. I urge your approval and transmittal to the Congress.

Cordially,

Sean O'Keefe

**Enclosure:
As Stated**

APPENDIX A: LEGISLATION PROPOSED BY THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE (cont'd)

(General Provision)

Ser. _____. During the current fiscal year, in the case of a fixed appropriation account of the Department of Defense for fiscal year 1992 and prior fiscal years, whose period of availability for obligation has ended but which has not been closed under section 1552(a) of title 31, United States Code, obligations and adjustments to obligations that would have been properly chargeable to that account, but for which sufficient obligational authority is not available in that account, may be charged to a current appropriation account of the Department of Defense available for the same purpose: Provided, That charges to current appropriations may not be made under this section until the Committees on Appropriations and Armed Services of the Senate and the House of Representatives have been notified of the intention to make such charges and a period of 30 days has elapsed after the notice is submitted.

Purpose of the Legislation

Currently, Public Law 101-510, November 5, 1990, authorizes use of a current (unexpired) appropriation account for obligations and adjustments to obligations of a closed account five years after expiration. However, a similar provision was not included for obligations and adjustments to obligations of an expired account within the five year period.

The proposed legislation would result in similar treatment of expired accounts and closed accounts. The legislative proposal would authorize the use of a current (unexpired) account that is available for the same purpose as the expired account for recording obligations and adjustments to obligations that, if sufficient obligational authority existed, would have been properly chargeable to the expired account. In the absence of such authority, a separate appropriation would be necessary to provide the required obligational authority prior to the payment of applicable amounts.

**APPENDIX B: APPROVED LEGISLATION, NATIONAL DEFENSE AUTHORIZATION ACT
FOR FISCAL YEAR 1993**

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quired by section 1406 of the National Defense Authorization Act for Fiscal Year 1991 (Public Law 101-510; 104 Stat. 1680) have been completed.

SEC. 1004. ADDITIONAL TRANSITION AUTHORITY REGARDING CLOSING APPROPRIATION ACCOUNTS.

Section 1405(b) of the National Defense Authorization Act for Fiscal Year 1991 (31 U.S.C. 1551 note) is amended by adding at the end the following new paragraph:

"(8) OBLIGATIONS AND ADJUSTMENTS OF OBLIGATIONS FOR EXPIRED BUT NOT CLOSED ACCOUNTS.—(A) Subject to subparagraphs (B), (C), and (D), in the case of an appropriation account for a fiscal year before fiscal year 1993 for which the period of availability for obligation has expired but which has not been closed under the provisions of section 1552(a) of title 31, United States Code, or paragraph (4) of this section, an obligation and an adjustment of an obligation may be charged to any current appropriation account of the Department of Defense that is available for the same purpose as the expired account if—

"(i) the obligation would have been properly chargeable (except as to amount) to the expired account before the end of the period of availability of that account; and

"(ii) the obligation is not otherwise properly chargeable to any current appropriation account of the Department of Defense.

"(B) The total amount charged to a current appropriation account under subparagraph (A) may not exceed an amount equal to the lesser of—

"(i) one percent of the total amount of the appropriations for that account; or

"(ii) one percent of the total amount of the appropriations for the expired account.

"(C) No obligation or adjustment of an obligation may be charged pursuant to the provisions of this paragraph until the Committees on Armed Services and the Committees on Appropriations of the Senate and House of Representatives are notified of the intent to make such a charge and a period of 30 days elapses after the notification is submitted.

"(D) CERTIFICATIONS.—No obligation or adjustment of an obligation may be charged pursuant to the provisions of this paragraph until the Secretary of Defense (except as otherwise provided in subparagraph (E)) certifies to Congress the following:

"(i) That the limitations on expending and obligating amounts established pursuant to section 1341 of title 31, United States Code, are being observed within the Department of Defense.

"(ii) That reports on any violations of such section 1341, whether intentional or inadvertent, are being submitted to the President and Congress immediately and with all relevant facts and a statement of actions taken as required by section 1351 of title 31, United States Code.

"(E) ALTERNATIVE TO CERTIFICATION.—If the Secretary of Defense is unable to make the certifications referred to in sub-

**APPENDIX B: APPROVED LEGISLATION, NATIONAL DEFENSE AUTHORIZATION ACT
FOR FISCAL YEAR 1993 (cont'd)**

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paragraph (D) within 60 days after the date of the enactment of this subparagraph, the Secretary shall submit to the Congress a report stating that the Secretary is unable to make such certifications and setting forth the actions that the Secretary will take in order to enable the Secretary to make such certifications after the end of that period."

SEC. 1005. CLARIFICATION OF SCOPE OF AUTHORIZATIONS.

No funds are authorized to be appropriated under this Act for the Federal Bureau of Investigation.

SEC. 1006. INCORPORATION OF CLASSIFIED ANNEX.

(a) **STATUS OF CLASSIFIED ANNEX.**—The Classified Annex prepared by the Committee of Conference to accompany the conference report on the bill H.R. 5006 of the One Hundred Second Congress and transmitted to the President is hereby incorporated into this Act.

(b) **CONSTRUCTION WITH OTHER PROVISIONS OF ACT.**—The amounts specified in the Classified Annex are not in addition to amounts authorized to be appropriated by other provisions of this Act.

(c) **LIMITATION ON USE OF FUNDS.**—Funds appropriated pursuant to an authorization contained in this Act that are made available for a program, project, or activity referred to in the Classified Annex may only be expended for such program, project, or activity in accordance with such terms, conditions, limitations, restrictions, and requirements as are set out for that program, project, or activity in the Classified Annex.

(d) **DISTRIBUTION OF CLASSIFIED ANNEX.**—The President shall provide for appropriate distribution of the Classified Annex, or of appropriate portions of the annex, within the executive branch of the Government.

Subtitle B—Naval Vessels and Related Matters

SEC. 1011. EAST COAST HOMEPORT FOR NUCLEAR-POWERED AIRCRAFT CARRIERS.

(a) **FINDINGS.**—Congress finds that—

(1) Mayport, Florida, has served well as a homeport for aircraft carriers;

(2) under existing carrier force structure plans, as conventionally fueled aircraft carriers are replaced by nuclear-powered aircraft carriers, there will be a requirement for a second East Coast homeport for nuclear-powered aircraft carriers (in addition to the existing homeport of Norfolk, Virginia); and

(3) Mayport ought to be the second East Coast homeport for nuclear-powered aircraft carriers, when such additional homeport becomes needed.

(b) **DEVELOPMENT OF SECOND HOMEPORT.**—Not later than April 1, 1993, the Secretary of the Navy shall submit to the congressional defense committees a report on the Navy's plan for developing a second East Coast homeport for nuclear-powered aircraft carriers. The report shall include a schedule, by fiscal year, for funding the development of a second homeport for nuclear-powered aircraft carriers on the East Coast of the United States. The schedule shall be

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN

ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN

EXECUTIVE SUMMARY

On April 6 & 9, 1992, the Air Force terminated portions of one of its contracts with General Dynamics/Convair for the production of the AGM-129 Advanced Cruise Missile (ACM). The terminated portions involve missiles authorized for the FY87 and FY88 production lots. The contract is Fixed Price Incentive and, for each program year, funded to target price. The partial termination was necessary because sufficient funds in excess of those previously obligated for the target price of the contract were not available to complete these portions of the contract. The Air Force reduced the FY87 and FY88 production effort to stay within the available funds. Unfinished work in process became government property.

General Dynamics will complete work on the terminated residual missiles from FY87 and FY88 under a new FY92 contract. This course of action will result in delivery of the missiles needed to meet the Air Force's requirements without significant schedule impact. Some cost growth may result due to termination settlements and new negotiations for the FY92 missiles. The remaining FY92 ACM funds will be used to complete the procurement of the required support for the 820 missile fleet.

SYSTEM DESCRIPTION

The Advanced Cruise Missile is a subsonic, turbofan-powered, winged vehicle designed for carriage and launch from the B-52H aircraft. The ACM design takes full advantage of existing cruise missile technology (AGM-86B/AGM-109) and "state of the art" stealth characteristics. It provides significantly increased weapon system capability over the AGM-86B ALCM in operational range, standoff range, accuracy, mission planning flexibility, and survivability.

PRIOR YEAR FUNDING SHORTFALL

The funding shortfalls are identified for the FY87/88 ACM production contract with General Dynamics, Convair division (GD/C). These two production

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

lots are covered under the same contract definitized in FY88. This contract is Fixed Price Incentive Firm (FPIF) and each production effort has a negotiated target cost, target profit, ceiling price and overrun/underrun share ratio. The nature of this contract implies some degree of technical, schedule, and cost risk. The Air Force obligated funds to cover the most probable price, which was the target price. All allowable costs of effort expended to achieve the contents of the contract up to ceiling price are fully billable to the government. Engineering change proposals (ECPs) which affect the contract schedule, whether negotiated or accepted as "no change to target cost," are billable to the government in accordance with the provisions of the contract pricing structure. Costs for ECPs which are added to the contract at no increase in target price and ceiling price are billable to the government with the designated share ratio, in this case 70/30 where the contractor shares 30 percent of this cost, until ceiling price is reached. All costs over the ceiling price are borne solely by the contractor. Specific missile problems that led to the shortfall follow.

FUEL BLADDER PROBLEM: In early 1990, numerous fuel leaks were detected in missiles delivered to KI Sawyer AFB and were attributed to the fuel bladder material. Extensive redevelopment efforts followed at GD/C resulting in a new bladder design/material. Deliveries of missiles were delayed approximately six months awaiting this development, qualification testing, and subsequent incorporation into the production/retrofit process. This new bladder was implemented via a contract change to update part numbers, technical orders (TOs), etc. Redesign and retrofit of bladders was provided at no increase in contract target price or ceiling price.

Based upon Cost Performance Reporting (CPR) Analysis, both FY87 and FY88 lots were still forecasted to stay within available funding. However in April, 1991, additional problems were identified resulting in the decision to stop accepting missiles from GD/C. The following paragraphs detail the problems causing the actual funding shortfall.

NEW SEALING CRITERIA: Missile sealing requirements were modified after some fielded missiles showed signs of water intrusion (corrosion) into the engine cavity. The revised test specifications were implemented via a contract change at no increase in contract target or ceiling price.

WING DEPLOYMENT ACTUATOR (WDA): The WDA was redesigned after fluid leakage was found in several missiles, potentially impacting missile wing

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

deployment during flight. The redesign was implemented via a contract change to update part numbers, TOs, etc. at no increase to contract target price or ceiling price.

SCHEDULE SLIPS TO IMPLEMENT QUALITY FIXES: Nineteen quality problems were identified as critical issues by the user, Strategic Air Command (SAC). Incorporation of the fixes to these problems in the production/retrofit process impacted the manufacturing and delivery schedule at GD/C. A new delivery schedule was implemented by a contract change in Oct 1991. This work was incorporated into the contract at no increase in contract price or ceiling price.

IDENTIFICATION OF QUALITY PROBLEMS AND PROPOSED FIXES: This effort included the identification of quality problems, inspecting work-in-process, modifying manufacturing procedures, and developing work force training on problem areas such as safety wire and cotter pins.

IN-PLANT RECEIPT INSPECTION (IPRI): This factory simulation of the field receipt inspection was instituted to identify and eliminate missile deficiencies before reaching SAC. Corrective actions were subsequently incorporated into the manufacturing process to drive the deficiencies out. This is a short term effort initiated by the contractor to improve overall missile quality.

INITIAL SPARES: The cost of the ACM production asset was affected by all the events listed above. Initial spares shared in that cost up to the ceiling price of that requirement which was separately negotiated and funded by Oklahoma City Air Logistics Center (OCALC).

These problems resulted in a determination that both the FY87 and FY88 buys, now expired funds, would go to the ceiling price. Sourcing the funding shortfall would be determined by policy governing use of expired funds. Under financial management regulations which were in effect when these contracts were awarded, adequate funds would have been available to cover these shortfalls from the Merged or "M" account. New Congressional direction has prevented access to funding under these procedures by requiring that the source funds for such shortfalls be the same fiscal year and appropriation as the original contract funding. The Air Force did not have adequate funds available to cover the FY87 or FY88 need. For the FY87 buy the 8020 government share between ceiling and target price is \$81.6M. For the FY88 buy the government's share is \$30.7M. For each production lot the contractor's costs were expected to exceed the ceiling price. A cost breakout is Attachment 1.

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

CONTRACTING STRATEGY

BACKGROUND: General Dynamics/Convair (GD/C) was the original developer of the ACM system and was awarded production contracts beginning with the FY85 lot. The FY87 contract for 150 missiles, delivered 54 completed missiles as of April 6th. This FPIF contract estimate at completion was over target cost and Government liability was calculated on a 70/30 share ratio as the contract approached selling. The FY87 and FY88 production efforts are covered by this single contract. Since the Air Force identified this funding deficiency, attempts to obtain FY87 funding or approval to use current year funds to cover this liability have been disapproved.

ACTIONS TAKEN: On April 6, 1992, the FY87 production effort had reached the point where the termination liability for FY87 was equal to the total obligated FY87 funding. The Air Force proceeded with an immediate termination to preclude a violation of the Anti-Deficiency Act. Although not as immediate, the FY88 production effort was also forecast to reach its funding limit. Based on the knowledge that no additional FY88 funds were available and the use of current year funds was disapproved, action was taken to terminate FY88 missiles to preclude a deficient funding situation on the FY88 effort. In order to minimize disruption to other existing contracts and the cost impact of these terminations, a letter contract was issued to GD/C on April 6, 1992, to complete the 96 terminated missiles from the FY87 production lot. The letter contract was amended on April 9th to include 24 terminated missiles from the FY88 production lot, for a total of 120 missiles to be completed using FY92 8020 funds (Attachment 2). The completion and delivery of these missiles began immediately and will conform to the schedules previously negotiated for the FY87 and FY88 missile production lots. The definitized contract for these 120 missiles will reflect appropriate terms and conditions of the FY90/91 contract recently negotiated and all clauses required by the Federal Acquisition Regulations (FAR) on the date of execution of the letter contract. These actions minimize further cost growth, the number of terminated missiles, and maintain the current production rate to meet SAC's Required Asset Available date.

COST RISK: The cost risk for this FY92 production buy is considered low. Since the FY87 terminated missiles are nearly complete, the remaining effort, which will be completed under this FY92 contract is a small portion of the missile build activity. All FY88 terminated missiles require fabrication and assembly.

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

SCHEDULE RISK: Schedule risk is considered low, since this effort uses terminated material which was largely completed under the FY87/88 production effort.

COMPETITION: Competition has been actively pursued throughout the ACM Dual Source production effort. McDonnell-Douglas Missile Systems Company (MDMSC) was determined to be a qualified "build to print" producer in January, 1991, and will produce 100 missiles of the FY90/91 production lots. However, based on the availability of existing assets and the decision to minimize total program costs, competition of this effort was not practical.

The authority to negotiate on an "other than full and open competition basis" is necessary due to unusual and compelling urgency. Awarding GD/C a sole source contract to use the terminated materials (partially completed missiles) as Government furnished materials and complete them on the FY87/88 contract schedule, avoided serious injury to the Government. These injuries would be in the form of substantial delays in satisfying the Required Assets Availability date, still a firm requirement for the weapon system; extreme termination costs and cost growth for these terminated missiles; and subsequent cost growth to the FY90/91 contract under the interdependency clauses in that contract. Failure to award the April 8th letter contract to complete the terminated missiles would have caused severe impact to the industrial base through at least an 11 month production break at GD/C which would result in more than 700 production workers being laid off. Not only would this result in a very high termination cost, but also have a severe cost impact to all follow-on missile production contracts. In addition to the cost impacts of stopping the production line to conduct the competition, the costs to allow MDMSC to build these missiles are prohibitive. A MDMSC award would require a nearly impossible task of identifying, preserving, packing, storage and shipping GD/C work in process and the substantiating paperwork. Additionally, significant rework of some of the materials and MDMSC repurchase of the terminated materials unique to the GD/C manufacturing process would provide delays of over 2 years to the ACM program with no benefit to the Government. These costs would make a second source proposal non-competitive from a cost standpoint. Therefore, full and open competition was not practical.

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

USE OF THE FY92 PROCUREMENT FUNDS

The budget authority for the ACM program is as follows:

	<u>APPROP</u>
FY92 MISSILE PROCUREMENT	433.2
FY91 ADVANCE BUY	88.3
FY92 ADVANCE BUY	68.1
MODIFICATION	13.0
INITIAL SPARES	6.8
REPLENISHMENT SPARES	<u>18.9</u>
TOTAL BUDGET AUTHORITY	634.3

The ACM program as a whole is not being terminated; the program is being concluded with a reduced missile quantity. There are some efforts within the ACM program that are being terminated, and other efforts that must be concluded to ensure the readiness and reliability of the missiles already produced or on contract. The following list of items includes both costs for terminated efforts and costs to conclude necessary work. It reflects the Government's reasonable estimate of finishing the ACM production program. Excluded are budgeted costs to complete development (3600 funds) of organic depot repair capabilities. Please note that some of the figures are estimates and may change depending on the results of incomplete negotiations.

This close out of the ACM program will require the Air Force to deal with the following costs:

<u>Item</u>	<u>Cost (\$M)</u>
130 OFE FY87/88 Missiles	135
Material Termination Liability (for FY92 buy)	194
Material Termination Liability (for FY93 buy)	16
Contractor Shutdown (planned for FY95)	60

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

**ATTACHMENT ONE
ACM FUNDING SHORTFALL EXPLANATION
(\$ IN M)**

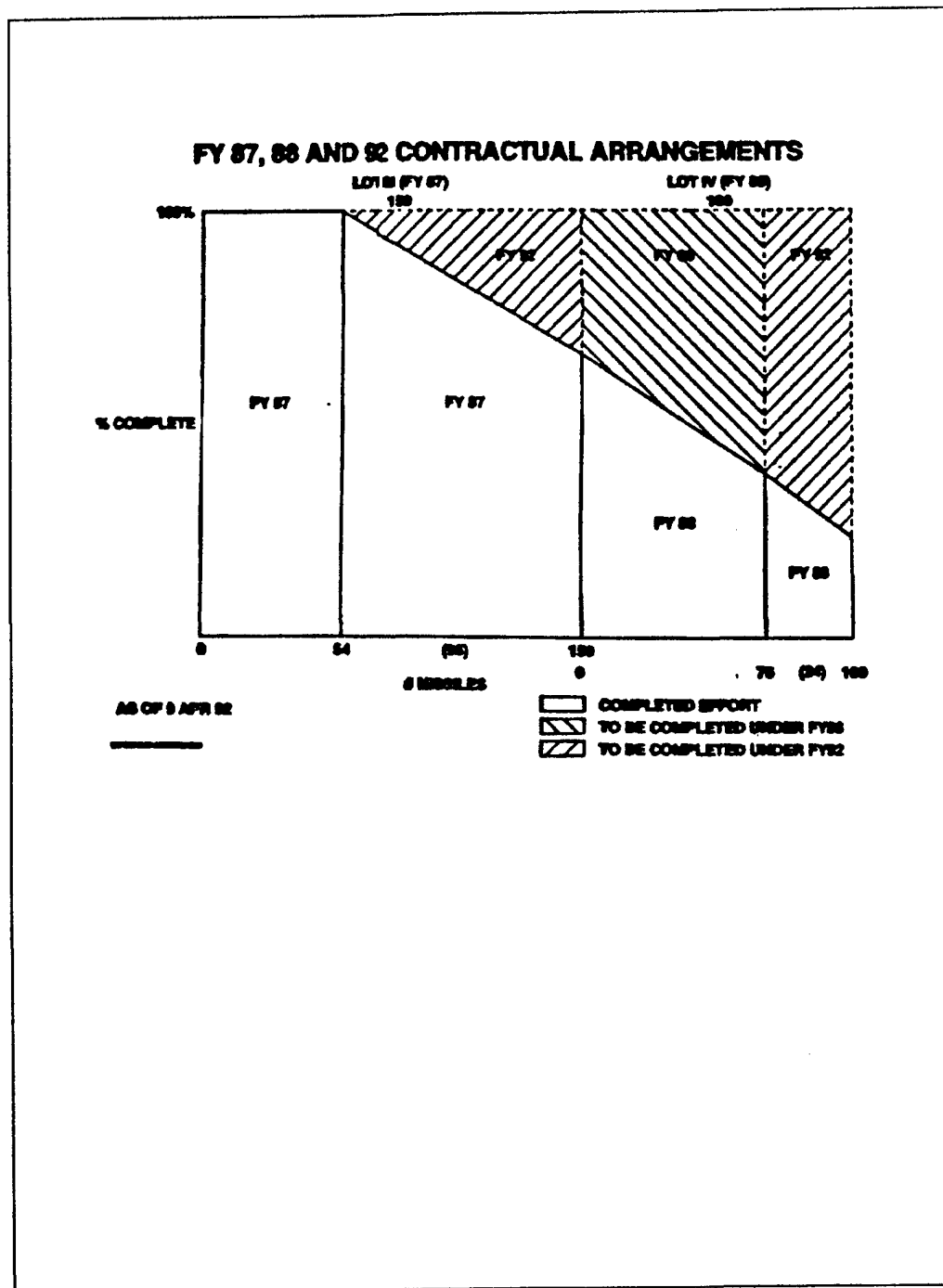
	FY87	FY88
<u>FUNDING SHORTFALL FOR OVERRUNS</u>	81.5	30.7
(Difference between ceiling and funded - 2020 funding)		
<u>CONTRACT CHANGES (All also increase in total cost)</u>		
FUEL BLADDER PROBLEM	10.4	4.4
RETROFIT FOR QUALITY PROBLEMS	0.4	
NEW SEALING CRITERIA (LEAK PROOF MISSILE)	23.2	11.9
WING DEPLOYMENT ACTUATOR	2.4	
SCHEDULE SLIPS TO IMPLEMENT QUALITY FIXES	19.8	1.9
MISCELLANEOUS MINOR CHANGES	1.8	
TOTAL CONTRACT CHANGES	58.0	18.2
<u>CONTRACT PROCEDURAL CHANGES (Within scope of original contract)</u>		
IN-PLANT RECEIPT INSPECTION	2.7	0.1
ID OF QUALITY PROBLEMS & PROPOSED FIXES	25.8	34.1
TOTAL PROCEDURAL CHANGES	28.5	34.2
TOTAL PROCEDURAL & CONTRACT CHANGES	86.5	52.4
CONTRACTOR OUT OF POCKET/OVER CEILING	-5.0	-21.7

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)

Sustaining Production Support (planned for FY93-95)	49
Test Instrumentation Payloads (planned for FY93-95)	82
820 Missiles Logistical Support (planned for FY93-95)	86
TOTAL REQUIREMENTS (FY92)	\$862M

This current estimate indicates the ACM FY92 budget authority for missile procurement will provide the necessary funding. It does include a significant management challenge that actually exceeds the cost estimate. Any significant reduction in the budget authority will result in a further reduction in missile quantity or the generation of an unfunded requirement in FY93-96 to complete the logistical support for the 820 missile fleet previously planned for later years in the production cycle.

APPENDIX C: ADVANCED CRUISE MISSILE PROGRAM CLOSEOUT PLAN (cont'd)



APPENDIX D: SUMMARY OF POTENTIAL BENEFITS RESULTING FROM AUDIT

<u>Recommendation Reference</u>	<u>Description of Benefit</u>	<u>Type of Benefit</u>
A.1., A.2., A.3., A.7., A.8.	Compliance. Proposed policies and procedures will improve fiscal accountability and management of Defense appropriations.	Nonmonetary.
A.4., A.5., A.6.	Compliance. Proposed policies and procedures will improve reliability of DoD's accounting data.	Nonmonetary.

APPENDIX E: ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Comptroller of the Department of Defense
Defense Finance and Accounting Service-Denver Center,
Denver, CO

Department of the Air Force

Assistant Secretary of the Air Force (Acquisition)
Assistant Secretary of the Air Force (Financial Management and
Comptroller)
Air Force Materiel Command (formerly Air Force Logistics and Air
Force Systems Command)
Headquarters, Andrews Air Force Base, MD
Headquarters, Wright-Patterson Air Force Base, OH
Aeronautical Systems Division (South), Eglin Air Force
Base, FL
Space Systems Division, Los Angeles Air Force Base, CA
Ogden Air Logistics Center, Hill Air Force Base, UT
Ballistic Missile Office, Norton Air Force Base, CA

APPENDIX F: REPORT DISTRIBUTION

Office of the Secretary of Defense

Comptroller of the Department of Defense
Director, Defense Finance and Accounting Service
Director, Defense Finance and Accounting Service,
Denver Center

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and
Comptroller)
Commander, Air Force Materiel Command, Wright-Patterson Air Force
Base, OH
Commander, Aeronautical Systems Division (South), Eglin Air Force
Base, FL
Commander, Space Systems Division, Los Angeles Air Force Base, CA
Commander, Ogden Air Logistics Center, Hill Air Force Base, UT
Commander, Ballistic Missile Office, Norton Air Force Base, CA

Non-DoD Agencies

Office of Management and Budget
General Accounting Office

Chairmen and Ranking Minority Members of the following
Congressional Committees:

Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security,
Committee on Government Operations

PART IV: MANAGEMENT COMMENTS

Comptroller of the Department of Defense
Air Force

MANAGEMENT COMMENTS: COMPTROLLER OF THE DEPARTMENT OF DEFENSE



OFFICE OF THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON DC 20301 1100

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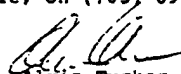
MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, ODODIG

SUBJECT: Draft Report on the Audit of Missile Procurement
Appropriations for the Air Force (Project
No. 2FG-5001)

An IG, DoD memorandum, dated September 9, 1992, requested the DoD Comptroller provide comments on the subject draft report in order that the comments may be considered in preparing the final report.

Generally, this office concurs or partially concurs in the findings and recommendations. Attached are specific responses to each of the recommendations.

Questions concerning this matter may be directed to my action officer, Mr. De W. Ritchie, on (703)-697-0585.


Alvin Tucker
Deputy Comptroller
(Management Systems)

Attachment

MANAGEMENT COMMENTS: COMPTROLLER OF THE DEPARTMENT OF DEFENSE
(cont'd)

COMPTROLLER OF THE DEPARTMENT OF DEFENSE COMMENTS
ON A DoDIG DRAFT REPORT ON THE AUDIT OF MISSILE PROCUREMENT
APPROPRIATIONS FOR THE AIR FORCE (PROJECT NO. 2FG-5001)

Recommendation 1. The Comptroller, DoD, should investigate the Air Force's violation of the Antideficiency Act, fix responsibility, and comply with the reporting requirements of DoD 7200.1.

DoD Comptroller Response. Partially concur. The DoD Comptroller in a memorandum, dated July 15, 1992, requested the Air Force to investigate potential Antideficiency Act violations; provide quarterly progress reports to the Defense Finance and Accounting Service; and, if a violation is determined to have occurred, identify those personnel responsible. Also, the DoD Comptroller in a memorandum, dated July 15, 1992, requested the Defense Finance and Accounting Service to monitor the investigation closely.

If an ongoing investigation confirms that a violation of the Antideficiency Act has occurred, the Department will comply with the reporting requirements of DoD Directive 7200.1.

Recommendation 2. The Comptroller, DoD, should seek legislation to give reprogramming authority to use current year appropriations to pay obligations from expired years; when this authority is exercised because of deficient year accounts, notify Congress that a violation of the Antideficiency Act exists.

DoD Comptroller Response. Concur. In a letter to the Office of Management and Budget, dated April 30, 1992, the DoD Comptroller requested legislation that would authorize the use of current appropriations for obligations and adjustments for prior year programs.

During the first week of October 1992, the Congress passed a provision--Section 1004, "Additional Transition Authority Regarding Closing Appropriation Accounts"--that authorizes the Department to charge any current appropriation account of the Department of Defense that is available for the same purpose as the expired account under certain circumstances.

Additionally, Section 1004 requires the Secretary of Defense to certify to the Congress that reports of violations of section 1341 of title 31, United States Code, whether intentional or inadvertent, are being submitted to the Congress immediately and with all relevant facts and a statement of actions taken.

MANAGEMENT COMMENTS: COMPTROLLER OF THE DEPARTMENT OF DEFENSE
(cont'd)

Recommendation 3. The Comptroller, DoD, should require budget activities to report and promptly process upward obligation adjustments from expired years when these adjustments have been approved and are within the scope of the contract.

DoD Comptroller Response. Concur. This is a current DoD requirement in Section B, Chapter 93 of the DoD Accounting Manual.

Recommendation 4. The Comptroller, DoD, should direct the Air Force to fund within-scope obligation adjustments from expired years for the Advanced Cruise Missile, Titan IV, and Advanced Medium-Range Air-to-Air Missile from expired appropriations until legislative relief is provided.

DoD Comptroller Response. Partially concur. Within-scope adjustments associated with target-to-ceiling increases should be funded from expired accounts. However, consistent with DoD guidance current at that time, within-scope contract changes involving additional work should be funded from [then] current appropriations if the changes were approved between June 13, 1991, and April 19, 1992.

Recommendation 5. The Comptroller, DoD, should direct that all approved upward obligation adjustments from expired years (commitments or obligations) be included in "Reports on Budget Execution" (DD Forms 1176) to assure full visibility of expired year financial activity.

DoD Comptroller Response. Concur. This is a current DoD requirement in Section B, Chapter 93 of the DoD Accounting Manual.

Recommendation 6. The Comptroller, DoD, should accelerate plans to resolve problems with negative unliquidated obligation. At a minimum, these plans should require that a single record be used to account for funds and pay bills, and should require the disbursing station to ensure that funds are available before payment is made.

DoD Comptroller Response. Concur. The DoD Comptroller agrees with the need for the recommended actions. However, to use one record to both account for, and pay, amounts requires significant changes in both processes and systems. There is considerable doubt that actions needed to fully implement this recommendation can be accomplished in the immediate future no matter how desirable.

Nevertheless, the Office of the DoD Comptroller has requested each of the DoD Components to prepare, and submit to the Defense Finance and Accounting Service, a plan to take those actions which are

MANAGEMENT COMMENTS: CONTROLLER OF THE DEPARTMENT OF DEFENSE
(cont'd)

currently feasible to reduce undistributed disbursements and eliminate negative disbursements. The DoD Comptroller requested that applicable plans (1) identify needed changes to existing accounting systems to minimize undistributed disbursements, (2) identify future actions to preclude subsequent increases, and (3) include a timetable for accomplishing these actions. The Defense Finance and Accounting Service should be reviewing and implementing those plans as feasible.

In addition, the Defense Finance and Accounting Service, in conjunction with the Military Departments and Defense Logistics Agency, has established the Joint Contract Accounting and Finance Process Review Group to develop short-term and cost-effective fixes, and examine and develop policy proposals to resolve process problems. The Group is drafting reporting requirements to monitor the progress being made in reducing negative unliquidated obligations.

Recommendation 7. The Comptroller, DoD, should revise DoD accounting policy to allow program managers to rely on best cost-to-ceiling estimates and adjust these obligations as more data become available.

DoD Comptroller Response. Partially concur. It must be assumed that "target" prices represent "best-cost estimates" at the time a contract is awarded. If the target price is too low or too high, the target price should be adjusted, upward or downward, to reflect the best-cost estimate. Subsequent to entering into a contract, if the "best-cost estimate" varies from the initial "target" price, appropriate adjustments to obligated amounts should be made.

Nevertheless, the guidance in Chapter 25, paragraph D.2., of the DoD Accounting Manual will be revised to explicitly provide for obligations to be adjusted above or below a target or billing price stated in the contract. The Defense Finance and Accounting Service will be requested to include revised guidance, as shown below, in the DoD 7000.14-R, "DoD Financial Management Regulation" (supersedes the DoD Accounting Manual) by March 31, 1993:

2. Fixed-Price Contract With an Escalation, Price Redetermination, or an Incentive Provision. When a contract is awarded, an obligation must be recorded for the amount of the target or billing price stated in the contract, even though the contract may contain a ceiling price in a larger amount. Subsequently, a target or billing price should be adjusted upward or downward to a "best-cost estimate" whenever it is determined that, and documentary evidence supports, the actual cost of the contract will differ materially from the original target or ceiling price stated in the contract.

MANAGEMENT COMMENTS: COMPTROLLER OF THE DEPARTMENT OF DEFENSE
(cont'd)

Recommendation 8. The Comptroller, DoD, should seek legislation to allow contingent liabilities (contractor incentives and award fees) to be funded from the missile procurement appropriation that is current when the contractor earns the fees.

DoD Comptroller Response. Partially concur. Under existing opinions of the Comptroller General, contingent liabilities arising from clauses originally contained in a contract are chargeable to the fiscal year when earned. The Department of Defense policy is to cover contingent liabilities such as incentive and award fees within appropriations authorized by the Congress. Limited relief has been provided in the National Defense Authorization Act, 1991, Public Law No. 101-510 and the National Defense Authorization Act, 1993, Public Law No. 102-484. These authorities permit charging current appropriations when sufficient funds do not exist in merged or expired accounts. Additional legislation is not needed at this time.

MANAGEMENT COMMENTS: DEPARTMENT OF THE AIR FORCE

Final Report
Page No.



OFFICE OF THE ASSISTANT SECRETARY

DEPARTMENT OF THE AIR FORCE
WASHINGTON DC



19 NOV 1992

MEMORANDUM FOR THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Air Force Comments on the DoD(IG) Report on the Audit of Missile Procurement Appropriations for the Air Force Project No. 2PG-5001- ACTION MEMORANDUM

While we have not been formally tasked to provide comments, we have taken the liberty of responding to the subject draft audit report. The following comments reflect changes in circumstances since the audit was conducted and comments regarding conclusions drawn in the report.

1. Page 7, para. 2: "The House Bill for FY 1993 Defense Appropriations provides that the Air Force shall reimburse the subcontractor an additional \$120 million as a matter of equity".

Recommend this paragraph be changed to reflect the provision that was contained in the 1993 Appropriations Act, Sec. 9164, "Notwithstanding any other provision of law, prior to March 1, 1993, the Secretary of the Air Force is directed to enter into a Supplemental Agreement to Air Force Prime Contract F04701-85-C-0019 for a Heavy Lift Expendable Launch Vehicle; Provided, That such a Supplemental Agreement shall address the Solid Rocket Motor Upgrade (SRMU) program and shall provide up to \$350,000,000 in payment to the prime contractor and the agreed upon payments to the subcontractor... That within funds appropriated to the Department of the Air Force either in this Act or in Public Law 102-172 not less than \$200,000,000 nor more than \$300,000,000 shall be available for the Supplemental Agreement...

In accordance with this provision, the Air Force will reprogram dollars for Titan IV to cover the claim for Hercules. The funds referenced in this Act and in Public Law 102-172 cover FY 1992 and FY 1993 appropriations. The claim will be covered with current appropriations. It does not represent an additional bill against the expired appropriation accounts.

2. Page 9, para. 1: "We estimate that as of March 31, 1992, the deficiencies were about \$119 million for FY 1987 and \$183 million for FY 1988."

These numbers include amounts for the Advanced Cruise Missile (ACM) program (\$111.5M for FY 1987, \$54.7M for FY 1988). These amounts should not be included in the estimates of prior year deficiencies. These adjustments were unnecessary after the partial termination of the FY 1987 and FY 1988 ACM contracts.

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MANAGEMENT COMMENTS: DEPARTMENT OF THE AIR FORCE (cont'd)

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3. Page 11, para. 1: "This proposed legislation would allow the use of current year funds; DoD Components would also be required to report any violations of the Antideficiency Act that required use of this authority."

Recommend this paragraph be changed to reflect legislation enacted as Section 1004, Title X, of the Defense Authorization Act of 1991. The legislation does, as the report states, allow the Services to use current appropriations to pay obligations which would have been properly chargeable to an expired appropriation account, but for which sufficient obligation authority is not available in that account. This provision is subject to limitations regarding reporting, duration and the requirement to follow existing Antideficiency statutes.

6

4. Page 12, table: FY 1987 AND 1988 DEFICIENCIES IN AIR FORCE MISSILE PROCUREMENT APPROPRIATIONS

Recommend the table be changed as follows:

FY 1987 AND 1988 POTENTIAL DEFICIENCIES IN AIR FORCE MISSILE PROCUREMENT APPROPRIATION ACCOUNTS (\$ millions)

Deficiencies	1987	1988
Approved upward obligation adjustments	\$ 30.0	\$ 65.2 1/
Unapproved upward obligation adjustments	1.0	15.3 2/
Funding issues	1.9	12.0 3/
Contingent liabilities		10.5 4/
Subtotals	\$ 39.1	\$107.1
Less available funds (as shown in "Reports on Budget Execution")	30.0	37.7
Potential Deficiency	\$ 9.1	\$ 69.4

1/ Titan IV adjustments approved Jul 2, 1992: 1987 - \$21.1M, 1988 - \$24.4M

AMRAAM adjustments approved Jul 2, 1992: 1987 - \$8.95M, 1988 - \$40.8M

2/ We have not received requests for approval for the following adjustments cited by the audit report: 1987 - AIM-9(\$.7M), PLANT 44(\$.2M); 1988 - TITAN IV(\$3M), Peacekeeper(\$9M), AIM-9(\$.4M); Tacit Rainbow(\$.06M)

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- \$4.1 million for ACM award fee should not be included in this table. These funds were already obligated on the FY 1988 contract prior to March 1992.
- 3/ Delete amounts for ACM of \$111.5M - 1987 and \$54.7M - 1988
Delete amounts for TITAN IV Stretch-out of \$15.1M - 1988 (the SECAF has been given authority under the FY 1993 Appropriations Bill to approve incremental funding for the TITAN IV program. The SECAF has not given approval, however, the phasing of costs related to the program stretch out is uncertain at this time.)
- 4/ Delete amounts for TITAN IV - (SECAF approval for incremental financing for TITAN IV may alter the fund cite of future Award and Incentive fees.)
The litigation amount for TITAN IV (Hercules) should be removed because the Air Force has been directed in the FY 1993 Appropriations Act to use FY 1992/93 3020 appropriations to cover the claim.

5. Page 15, table: **UNRECORDED BUDGET ADJUSTMENTS.**
Recommend deletion of the following from unrecorded budget adjustments table:

	<u>FY 1987</u>	<u>FY 1988</u>
TITAN IV adjustments	\$21.1M	\$24.4M 1/
AMRAAM	\$ 8.5M .5M	\$36.6M 4.2M 2/
Advanced Cruise Missile award fee	0	\$ 4.1M 3/

- 1/ The TITAN IV adjustment was approved by SAF/FM Jul 2, 1992. The obligation was posted in the account records as of Sep 30, 1992.
- 2/ The amount for AMRAAM Lot II is \$36,600,000, not \$36,200,000 as reflected in the audit report. The AMRAAM adjustments were approved by SAF/FM on Jul 2, 1992. With the exception of the AMRAAM Producibility Program, the contract liabilities were obligated on Aug 7, 1992. The FY 1988 AMRAAM Producibility Program liability was posted in the accounting system on Sep 30, 1992.
- 3/ These funds are obligated against the FY 1988 ACM contract to pay for pending award fees.

9

6. Page 16, para. 2: **Funding issues.** Recommend last sentence be changed as follows: The Jun 13, 1991 DoD(C) guidance required that all upward obligation adjustments which resulted from additional work to be funded with currently available appropriations. This guidance was reversed Apr 20, 1992 and all within-scope contract changes were required to be funded within the account of the adjustment. Since the change in guidance, the Air Force has not, nor planned to, fund any within-scope contract changes with currently available appropriations.

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7. Page 16, para. 3: Funding FY 1987 and 1988 obligations with FY 1992 and future year dollars. "In addition to expired year obligations that had not been recorded, field activities incorrectly approved or were in the process of approving upward adjustments of \$113.4 million in FY 1987 and \$113.4 million in FY 1988."

Recommend this paragraph be revised for accuracy.

First, field activities do not approve upward adjustments in excess of \$100,000. The Air Staff has approval authority and exercises this authority in accordance with legislation and policy guidance extant at the time of approval.

Second, the amounts included in the totals for ACM (\$111.5M - 1987 and \$54.7M - 1988) should be removed. The ACM amount is not an upward adjustment "incorrectly funded" with current appropriations. It is new effort, covered with new obligations in current FY 1992 appropriations. The new effort is a result of the partial termination of prior year contracts to avoid Antideficiency violations in prior year accounts. In addition, the maximum amount of the shortfall as estimated by the Air Force in March is \$81.5 million in FY 1987 and \$30.7 million in FY 1988. The actual cost of the shortfall for both years on the 1992 contract now has a not to exceed price of \$56.8 million; this is \$109.4 million less than the Dod(IG) estimate.

The \$1.9M in FY 1987 and the \$15.1 million for TITAN IV, \$10 million for AMRAAM and \$2 million for TITAN II in FY 1988 exceed the \$100,000 approval threshold and must be approved by SAF/FM. They have not been submitted for approval yet, but when they are they will be reviewed on the basis of current policy guidance regarding the proper funding of upward adjustments and statutory language affecting TITAN IV.

9

8. Page 17, Table: FY 1987 and 1988 OBLIGATIONS FUNDED WITH FY 1992 AND FUTURE YEAR DOLLARS

Recommend deletion of table for reasons cited in #7. In addition, the TITAN IV FY 1988 amount related to stretchout, should be \$15.1 million instead of \$46.7 million.

9

9. Page 17, para. 1: Advanced Cruise Missile (ACM) Reprourement. "Therefore, within-scope upward adjustments of \$111.5 million (from 1987) and \$54.7 million (from FY 1988) were inappropriately funded with FY 1992 dollars."

In March 1992, the Air Force estimated the funding shortfall to be \$81.5 million in FY 1987 and \$30.7 million in FY 1988. Both shortfalls are now on a 1992 letter contract with a not to exceed price of \$56.8 million. This shortfall was not inappropriately funded with FY 1992 dollars. These funds should not be included in the FY 1987 and FY 1988 category for upward adjustments. The Air Force did not use current year appropriations to cover prior year adjustments for the ACM. These prior year bills were mitigated through a partial termination of the FY 1987 and 1988 contracts for the ACM. As a result there was unfinished work on the missiles associated with the FYs 1987 and 1988 contracts. This work was included in a new

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contract which was covered with current FY 1992 funds for the ACM program. The Air Force does not believe the use of FY 1992 funds to be improper. It was a prudent decision to complete missiles which were left unfinished as the result of a requirement to take measures to avoid violating the Antideficiency statute.

10. Page 17, para. 2: TITAN IV Stretch-out. "Air Force officials stated that they planned to use FY 1992 funds to pay \$15.1 million of the \$46.7 million in cost growth for the remaining unlaunched TITAN IV missiles from FY 1988."

Section 9164 of the 1993 Appropriations Act states that "...the Secretary of the Air Force may use incremental funding for the restructured TITAN IV program under the existing contract for 41 vehicles". The stretch-out referred to in the report for TITAN IV relates to the existing contract and is therefore subject to the authority to incrementally fund. The basis for incremental funding will have to be determined in conjunction with DoD(C). Until this has been established, it is unclear as to how these costs will be allocated across the years of the program.

10

11. Page 18, para. 3: AMRAAM Lot II erroneous specifications. Change sentence 1 through 5 to read "In November 1991, program managers identified the possibility of a \$8 to \$24 million upward adjustment for the Hughes Lot II production contract. At the time negotiations were not finalized. Per DoD(C) guidance of Jun 13, 1991, \$23 million in FY 1991 funds were set aside to cover the liability. Negotiations were completed and a request for upward obligation of \$20 million submitted to SAF/PM on Sep 28, 1991. When the request was submitted, FY 1991 funds were recommended as the source based on DoD Comptroller policy in effect at the time the requirement was submitted.

10

12. Page 19, para. 2: Future year funding. "Titan IV program managers plan to charge \$116 million to FY 1992 and future years to pay for storage and engineering costs incurred when production of the missile was postponed."

Recommend paragraph be revised for reasons stated in #10. The 1993 Appropriations Act gives the Air Force the authority to incremental fund the TITAN IV contract for 41 vehicles. Until the basis for incremental funding has been established, it is unclear how the storage and engineering costs will be allocated across the years of the program.

11

13. Page 21, para. 1: "The MPAAF had at least \$32.1 million in contingent liabilities that should be paid with FY 1988 funds; liabilities expected in future years totaled an additional \$120 million. Contingent liabilities...must be funded in the same year the event occurs, until the appropriation is canceled."

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Recommend paragraph be changed to reflect following:
\$21.6 million of the identified contingencies is for TITAN IV mission success fees. Under an incremental funding arrangement, mission success fees will likely be a proper charge to future appropriations.

The reference to liabilities expected in future years of \$120 million are for the Hercules claim. The 1993 Appropriations Act directs us to cover this claim with FY 1992 and 1993 appropriations.

Recommend deletion of the statement that "Contingent liabilities be funded in the same year the event occurs." This is true in most cases, but in the case of TITAN IV, the FY 1993 Appropriations Act directs specific fund cites for contingent liabilities associated with the TITAN IV program.

14. Page 21, para. 2: Awards and incentives. "These obligations include "mission success fees" of \$21.6 million for Titan IV....Unless legislation is changed, these costs should be absorbed by expired year appropriations."

Recommend we change this paragraph to include new language in the 1993 Appropriations Act which grants authority to incrementally fund the TITAN IV program.

15. Page 22, para. 2: Solid Rocket Motor Upgrade. "It is not yet clear whether that provision will become law or if it does, which MPAAF appropriation years would be impacted."

Recommend updating this paragraph to indicate that the referenced provision became law in Section 9164 of the 1993 Appropriations Act. The MPAAF appropriation years impacted by the provision are FY 1992 and FY 1993.

12

16. Page 23, para. 2: Negative Unliquidated Obligations. Change first sentence to read, "Negative unliquidated obligations (NULOs) (except for progress payments and refunds) are errors that occur when a disbursing station makes a payment against a contract for which the accounting station's records show that money is either insufficient or unavailable. This situation is usually caused by the disbursing station making payment against the incorrect appropriation. Current procedures require the accounting station to accept and post the incorrect expenditure and request the disbursing station correct the problem."

14

17. Page 26, para. 2: "We support the legislation proposed by the Comptroller..."

This section should be changed to reflect the enactment of Section 1004 of the FY 1993 Defense Authorization Act. This provision will allow us to charge expired year obligations to current appropriations when insufficient funds exist in the expired accounts to cover valid obligations.

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18. Page 26, Recommendation 1. "Investigate the Air Force's violation of the Antideficiency Act, fix responsibility, and comply with the reporting requirements of DoD Directive 7200.1."

Concur in principle. We notified DFAS-DE of potential violations of the Antideficiency Act for TITAN IV and AMRAAM on Jul 2, 1992. DFAS-DE has requested Air Force Materiel Command to initiate investigations into both programs. Investigating officers have been appointed and the investigations are in progress. We will comply with the reporting requirements of DoD Directive 7200.1 are being observed.

14

19. Page 27, Recommendation 2. "Seek legislation to give reprogramming authority to use current year appropriations to pay obligations from expired years; when this authority is exercised because of deficient year accounts, notify Congress that a violation of the Antideficiency Act exists."

Concur, however, this Recommendation should be updated to reflect the passage of Section 1004 of the FY 1993 Defense Authorization Act.

14

20. Page 27, Recommendation 3. "Require budget activities to report and promptly process upward obligation adjustments from expired years when these adjustments have been approved and are within the scope of the contract."

We concur with this recommendation. SAF/FM will issue guidance to the field reemphasizing the requirement to post obligation promptly once they have been recognized and approved.

14

21. Page 27, Recommendation 4. "Direct the Air Force to fund within-scope obligation adjustments from expired years for the Advanced Cruise Missile, Titan IV, and Advanced Medium-Range Air-to-Air Missile from expired appropriations until legislative relief is provided."

Nonconcur and recommend this be deleted from the report. Actions have already been taken to either mitigate the adjustments or to post them to the proper expired account.

We disagree that there are within-scope obligation adjustments which should be funded from expired year accounts for the Advanced Cruise Missile. Actions were taken to partially terminate the prior year contracts. These actions were necessary to mitigate a potential violation of the Antideficiency Statute. After the termination was done, adjustments were no longer necessary to fund the FY 1987 and 1988 contracts to ceiling. A new letter contract was established to complete the missiles associated with the prior year contracts. This contract is for new work to complete the missiles associated with the prior year contracts. These contracts were for new work beyond the terminated contracts and were funded with new obligations against the FY 1992 appropriation.

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The upward obligation adjustments for TITAN IV and AMRAAM which were submitted to SAF/FM for approval were approved Jul 2, 1992. The obligations for these adjustments have been posted against the FY 1987 and FY 1988 appropriation accounts regardless of availability to cover them. We know that deficiencies exist in the FY 1987 and FY 1988 Missile Procurement accounts as a result of these obligation adjustments. We have initiated investigations into potential violations of the Antideficiency Act and will comply with the legislative provision in Section 1004 of the FY 1993 Defense Authorization Act to cover these obligations with current availability.

22. Page 27, Recommendation 5. Direct that all approved upward obligation adjustments from expired years be included in "Reports on Budget Execution" to assure full visibility of expired year financial activity.

The Air Force concurs with this recommendation. SAF/FM has already directed field activities to post all approved upward adjustments for incurred liabilities regardless of funds availability to cover them. In the situation where there are insufficient funds to cover adjustments posted, DFAS-DE has been notified of a potential violation of the Antideficiency Act. We consider this recommendation a closed issue.

15

23. Page 27, Recommendation 6. "Accelerate plans to resolve problems with negative unliquidated obligations."

We concur. The Defense Finance and Accounting Service established the Joint Contract Accounting and Finance Process Review Group in May 1991. The purpose of this group is to identify problems and develop solutions to improve the processes associated with accounting and paying DoD contracts paid by DFAS. It is a joint DFAS and DoD Component effort. The Air Force is represented by both Secretariat and MAJCOM personnel who are actively involved in the effort.

15

24. Page 28, Recommendation 7. "Revise DoD accounting policy to allow program managers to rely on best-cost to ceiling estimates and adjust these obligations as more data becomes available."

We concur with this recommendation. We are and will continue working with DoD(C) to readdress policies which discourage proper accounting for program liabilities.

15

25. Page 28, Recommendation 8. "Seek legislation to allow contingent liabilities (contractor incentives and award fees) to be funded from the missile procurement appropriation that is current when the contractor earns the fees."

Concur with this recommendation. Air Force will support in efforts to obtain legislation.

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26. Page 29. Finding B. **REPROCUREMENT OF ADVANCED CRUISE MISSILE.** "To avoid declaring a violation of the Antideficiency Act, Air force officials terminated contracts for the Advanced Cruise Missile (ACM) and initiated reprocurement actions the following day using FY 1992 funds...Furthermore, the Air Force actions did not avoid a violation of the Antideficiency Act."

Request deletion of this finding. The Air Force did not terminate ACM contracts to avoid declaring a violation of the Antideficiency Act. The fact is the Air Force took specific contract/program execution action to avoid incurring a violation.

United States Code, title 31, Section 1341 (a) (1), states, "An officer or employee of the United States Government may not --

(A) make or authorize an expenditure or obligation exceeding an amount in an appropriation or fund for the expenditure or obligation

(B) involve either government in a contract or obligation for the payment of money before an appropriation is made unless authorized by law."

Since the Air Force was unable to provide the ACM program office with additional FY 1987 or FY 1988 funding prior to the date on which contract termination liabilities equalled obligated amounts, any action allowing future expenditures to occur in excess of the amount obligated would be, in our opinion, a violation of Section 1341 (a) (1) (A) above. Responsible action to prevent a violation should not be considered action taken to avoid reporting a violation.

The contracting officer has the responsibility to manage individual contracts and to ensure funding is available to cover expected contract costs regardless of the status of total Air Force appropriation balances. The terminations were affected by the program office to preclude a violation of the law.

Immediately following the termination of the FY 1987 and FY 1988 procurement contracts for ACM in April, assets owned by the government from the terminated contracts were provided as Government Furnished Equipment (GFE) to the contractor to complete missiles authorized by Congress in the FY 1992 DoD Authorization Bill.

22

27. Page 31. para. 4. "Senior Air Force officials maintained that: it was legal to cancel a contract one day, create a new contract the next day, and fund FY 1987 and 1988 requirements with FY 1992 dollars;"

Recommend to accurately portray the tone and rationale behind the Air Force decision, this paragraph be altered for accuracy. The Air Force maintains that the action taken to partially terminate the prior year ACM contracts was the only

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legal option. Failure to terminate the contracts would have resulted in a violation of the Antideficiency statute. Once the termination of the prior year contracts took place, any additional effort related to the production of the associated missiles constituted new work and could be funded with current appropriations. Therefore, actions taken to create a new contract to complete the missiles were proper.

28. Page 32, para. 3. Potential for increased liability. "In our opinion, the Air Force's procurement actions were incorrect because the cost growth on the ACM contract did not result from scope changes or new work and the costs were properly chargeable only to FY 1987 and FY 1988 funds."

Recommend that this statement be deleted. Once the FY 1987 and FY 1988 contracts for ACM were terminated, any effort to

complete the missiles associated with the terminated contracts constituted new work.

22

29. Page 32, para. 3: Potential for increased liability. "Because of the new ACM contracts, the Air Force may have to pay an additional \$49 million in contract termination costs and liabilities that would have been absorbed by the contractor under the original contracts."

Recommend this assertion be removed. The DoD(IG) analysis is incorrect. The Air Force action precluded a break in the production line of up to 11 months, saved significant production downtime costs, and limited any termination related costs to approximately \$4 million. As of March 1992, the Air Force estimated funding shortfall on ACM was \$81.5 million in FY 1987 and \$30.7 million FY 1988 vice \$111.5 million FY 1987 and \$54.7 million FY 1988 that the report identifies. This shortfall is now funded with FY 1992 funds with a NTE of \$56.8 million that will complete the 120 FY 1987 and FY 1988 missiles. This is \$109.4 million less than the original DoD(IG) assessment.

Hughes Missile Systems Company has agreed to complete the assembly and delivery of the 120 missiles that were terminated from the FY87/88 contract under a new firm fixed price arrangement that will not exceed the price we would have paid under the original negotiated contract ceiling price, which was the Air Force estimate at completion at the time the contract action was taken.

23

30. Page 34, para. 2: Conclusion "The Air Force may have breached its fiduciary responsibility by incurring additional costs in an attempt to avoid reporting a violation of the Antideficiency Act."

Recommend that this paragraph be revised to provide a more accurate account of the actions taken related to the ACM program. The Air Force terminated the FY 1987 and 1988 contracts to avoid incurring a violation of the Antideficiency Act. Furthermore, as

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stated above, the total cost of the 120 missiles will not exceed the original negotiated contract ceiling price, which was the Air Force estimate at completion at the time the contract action was taken.

31. Page 34. para. 2: **Conclusion** "The decision of the Assistant Secretary of the Air Force (Financial Management and Comptroller), (SAF/FM), does not make decisions regarding program content or management. He advises on the financial status of the appropriation accounts and the ability of these accounts to absorb anticipated upward obligation adjustments. This information is used by those responsible for programmatic decisions to develop options for managing the program within available funds."

This paragraph must be revised for accuracy. The Assistant Secretary of the Air Force (Financial Management and Comptroller), (SAF/FM), does not make decisions regarding program content or management. He advises on the financial status of the appropriation accounts and the ability of these accounts to absorb anticipated upward obligation adjustments. This information is used by those responsible for programmatic decisions to develop options for managing the program within available funds.

24

32. Page 35. para. 1: "Deficiencies in the FY 1987 and 1988 MPAAFs are unresolved, the Antideficiency Act has been violated, and the Air Force has incurred additional costs by not reporting Antideficiency Act violations and requesting Congressional relief."

Recommend this paragraph be updated for actions taken to date.

The Air Force agrees that both the FY 1987 and FY 1988 Missile Procurement account are deficient. It appears that the Antideficiency Act has been violated in at least two programs, TITAN IV and AMRAAM. We notified DFAS-DE of potential violations of the Antideficiency Act in these two programs in a Jul 2, 1992 memorandum. Investigations have been initiated and investigating officials assigned. We have requested, and received, Congressional relief for our deficient expired appropriation accounts. Section 1004 of the Defense Authorization Act allows charges to current appropriations when insufficient availability exists in these accounts to cover legitimate charges to these accounts. This provision does not remove the responsibility of reporting violations of the Antideficiency Act and we intend to meet its requirements.

SPECIFIC COMMENTS:

1

1. Page 1, para. 1: Insert "the old" before "M" on line 7. This distinction is necessary because the current "M" account still does fund upward obligation adjustments.

1

2. Page 1, para. 3: Insert "DoD" before "Comptroller" on the second line. Recommend this for clarity.

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1

3. Page 2, last para.: Insert "within-scope" before "contract changes" on the second line. Recommend this for accuracy.

2

4. Page 3, last para.: Delete "financial related" on the second line. Also, recommend changing "made" to "did" on the second line. Recommend this for clarity.

2

5. Page 3, last para.: Insert "(Det 24)" after "Division" and before "Eglin" on line 9. Recommend this for accuracy.

2

6. Page 4, para. 2: Insert "DoD" before "Comptroller" on line 1. Recommend this for clarity.

3

7. Page 6, para. 2: Insert "DoD" before "Comptroller" and delete "DoD" after "Comptroller" on line 10. Recommend this for easier reading.

4

8. Page 7, para. 1: Same change as #9 on line 2.

11

9. Page 20, para. 1: Change "expire" to "cancel" on line 2. Recommend this for accuracy. Also, change the second sentence to read "Instead funds are now available for upward obligation adjustments for 5 years versus indefinite availability under the old system when the accounts merged." Recommend this for clarity.

11

10. Page 21, para. 1: Change "can" to "must" on line 8. Recommend this for accuracy.

This concludes our comments to the subject audit report on the Fiscal Years 1987 and 1988 Missile Procurement accounts. The point of contact for questions regarding this input is Marilyn Thomas, SAF/FHBM, (703)695-4938.



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